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## A TREATISE

ON THE LAW OF

# PRIVATE CORPORATIONS

BY

WM. L. CLARK

AND

WM. L. MARSHALL

IN THREE VOLUMES VOL. II.

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### TABLE OF CONTENTS.

#### CHAPTER I.

DEFINITION AND NATURE OF A CORPORATION.
(For analysis in detail, see volume 1.)

#### CHAPTER II.

CLASSIFICATION OF CORPORATIONS. (For analysis in detail, see volume 1.)

#### CHAPTER III.

CREATION, NAME, AND EXISTENCE OF CORPORATIONS, AND THE AMENDMENT, EXTENSION, AND REVIVAL OF CHARTERS.

(For analysis in detail, see volume 1.)

#### CHAPTER IV.

EFFECT OF IRREGULARITIES IN ORGANIZATION, AND OF FAIL-URE TO INCORPORATE.

(For analysis in detail, see volume 1.)

### CHAPTER V.

PROMOTION OF CORPORATIONS; ACTS PRIOR TO INCORPORATION; INCORPORATION OF PARTNERSHIPS, ETC.

(For analysis in detail, see volume 1.)

#### CHAPTER VI.

CITIZENSHIP AND RESIDENCE OR DOMICILE OF CORPORA-

(For analysis in detail, see volume 1.)

#### CHAPTER VII.

POWERS OF CORPORATIONS IN GENERAL. (For analysis in detail, see volume 1.)

#### CHAPTER VIII.

POWER TO TAKE AND HOLD PROPERTY. (For analysis in detail, see volume 1.)

#### CHAPTER IX.

POWER TO TRANSFER OR INCUMBER PROPERTY AND FRANCHISES.

(For analysis in detail, see volume 1.)

#### CHAPTER X.

POWERS WITH RESPECT TO CONTRACTS.
(For analysis in detail, see volume 1.)

#### CHAPTER XI.

POWER TO TAKE AND HOLD STOCK. (For analysis in detail, see volume 1.)

#### CHAPTER XII.

EFFECT OF ULTRA VIRES AND ILLEGAL TRANSACTIONS. (For analysis in detail, see volume 1.)

#### CHAPTER XIII.

TORTS, PENALTIES, CRIMES, AND CONTEMPT OF COURT. (For analysis in detail, see volume 1.)

#### CHAPTER XIV.

ACTIONS BY AND AGAINST CORPORATIONS.
(For analysis in detail, see volume 1.)

#### CHAPTER XV.

LEGISLATIVE CONTROL OVER CORPORATIONS.
(For analysis in detail, see volume 1.)

#### CHAPTER XVI.

TAXATION OF CORPORATIONS. (For analysis in detail, see volume 1.)

#### CHAPTER XVII.

HOW CORPORATIONS MAY BE DISSOLVED; FORFEITURE OF CHARTER; EFFECT OF DISSOLUTION; WINDING UP UNDER STATUTORY PROVISIONS.

- I. How Corporations may Be Dissolved.
  - § 302. In general.
    - 303. Constitutionality of dissolution.
    - 304. Dissolution by act of the legislature.
      - (a) In general.
      - (b) Power to repeal charter.
      - (c) What constitutes repeal of a charter.
    - 305. Dissolution by expiration of time limited in charter.
    - 306. Dissolution by happening of prescribed contingency.
    - 307. Dissolution by failure or loss of integral part.
    - 308. Dissolution by surrender of charter.
    - 309. Suspension of business and nonuser of franchises.
      - (a) In general.

- (b) Failure to hold meetings.
- (c) Failure to elect officers.
- (d) Inability to continue business.
- 310. Alienation or loss of property and franchises.
- 311. Insolvency—Appointment of receiver—Bankruptcy proceedings—Assignment.
- II. FORFEITURE OF CHARTER AND FRANCHISES IN JUDICIAL PROCEEDINGS BY THE STATE.
  - § 312. In general.
    - 313. Necessity for judicial proceedings and judgment of forfeiture.
      - (a) In general.
      - (b) Nonperformance of conditions subsequent.
      - (c) Power of the governor.
    - 314. Grounds for forfeiture of a charter.
      - (a) In general.
      - (b) Misuser or abuse of franchises in general.
      - (c) Nonuser of franchises, neglect of duty, etc.
      - (d) Breach of conditions subsequent.
        - (1) In general.
        - (2) Substantial compliance with the charter or statute is sufficient.
        - (3) Construction in cases of doubt.
      - (e) Inutility or impracticability of the franchise or enterprise.
      - (f) Suspension or abandonment of business.
      - (g) Inability to continue business.
      - (h) Insolvency and failure to pay debts—Assignment for the benefit of creditors.
      - (i) Alienation of property.
        - (1) In general.
        - (2) Lease of property.
      - (j) Failure to hold meetings.
      - (k) Failure to keep or bring offices, officers, agencies, records, etc., within the state.
      - (1) Mere wrongful intent. .
      - (m) Defective organization.
      - (n) Subsequent compliance with the law.
      - (o) Particular penalty prescribed by the charter or statute.
      - (p) Fine or judgment of ouster.
      - (q) Acts and neglects of officers as acts and neglects of the corporation.
      - (r) Acts of stockholders as acts of the corporation.
    - 315. Waiver of forfeiture and estoppel of the state.
      - (a) In general.

- (b) In case of dissolution, ipso facto, on failure to comply with conditions.
- (c) Implied waiver.
- (d) Mere acquiescence and lapse of time.
- (e) Continuing cause of forfeiture.
- (f) Knowledge of cause of forfeiture.
- (g) Who may waive a forfeiture.
  - (1) In general.
  - (2) Waiver by a municipality.
- (h) Conditional waiver.
- (i) Violation of contract by the state.

#### III. PROCEDURE AND JURISDICTION.

- § 316. In general.
  - 317. Mode of procedure at common law.
  - 318. By what authority proceedings must be instituted.
  - 319. Jurisdiction of courts of equity.
  - 320. Statutory jurisdiction.
  - 321. Jurisdiction over foreign corporations.

#### IV. EFFECT OF DISSOLUTION.

- § 322. In general.
  - 323. Dissolution may be set up collaterally.
  - 324. When dissolution takes effect.
  - 325. Effect of dissolution with respect to franchises.
  - 326. Effect of dissolution with respect to debts and contracts.
    - (a) In general.
    - (b) Executory contracts.
    - (c) Contracts after dissolution.
    - (d) Offer before and acceptance after dissolution.
    - (e) Liability of stockholders or members.
  - 327. Effect of dissolution with respect to torts.
  - 328. Effect of dissolution with respect to property and conveyances.
    - (a) In general.
    - (b) The rule in equity applicable to modern business corporations.
    - (c) Statutory provisions for winding up.
    - (d) Transfer or assignment before dissolution.
    - (e) Conveyance to or by the corporation after dissolution.
    - (f) Conveyance in trust for the corporation.
  - Effect of dissolution with respect to actions and proceedings.
  - 330. Effect of dissolution on transfer of stock.

- V. CONTINUANCE AND WINDING UP UNDER STATUTORY PROVISIONS.
  - § 331. In general.
    - 332. Continuance of existence of corporations.
      - (a) In general.
      - (b) Collection of debts.
      - (c) Engaging in new business.
      - (d) Power to hold property.
      - (e) Disposal of property.
      - (f) Liability for torts.
      - (g) Actions and proceedings.
      - (h) Effect of statute on equity jurisdiction.
    - 333. Officers as trustees for creditors and stockholders.
      - (a) In general.
      - (b) Who are creditors.
      - (c) Property rights.
      - (d) Actions and parties thereto.
      - (e) Liability of officers as trustees.
    - 334. Appointment of receiver or trustee.
      - (a) In general.
      - (b) Appointment of successor.
      - (c) Appointment by governor or legislature.
      - (d) Where a trustee or receiver has been appointed by or with the consent of the corporation.
      - (e) Where the directors or other officers are made trustees.
      - (f) Where the existence of corporations is continued by statute.
      - (g) Time of application or appointment.
      - (h) Who may apply for a receiver.
      - (i) Who may be appointed receiver.
      - (j) Order appointing receiver.
      - (k) Effect of appointment.
      - (1) Transfer of property.
      - (m) Powers and duties of receivers.
      - (n) Temporary receiver.

#### CHAPTER XVIII.

# SUCCESSION OF CORPORATIONS; REORGANIZATION; CONSOLIDATION.

- I. SUCCESSION IN GENERAL; REORGANIZATION.
  - § 335. In general.
    - 336. Power to transfer property and franchises.
    - 337. Authority to reincorporate or reorganize.

- 338. Transfer as a dissolution.
- 339. Whether an old corporation is continued, or a new corporation created.
  - (a) In general.
  - (b) Reorganization creating a new corporation.
  - (c) Reorganization merely continuing old corporation.
  - (d) Extension or revival of charters.
  - (e) Amendment of charters.
  - (f) Grant of special charter to existing corporation.
  - (g) Change or retention of name.
- 340. Whether purchasers become a corporation.
- Property, rights, powers, franchises, and privileges of succeeding corporation.
  - (a) Property and rights in general.
  - (b) Powers, franchises, privileges, and immunities.
  - (c) Franchises passing with property.
  - (d) Strict construction in favor of the public.
  - (e) Rates chargeable by railroad companies, etc.
  - (f) Exemptions from taxation.
  - (g) Effect of constitutional prohibitions.
- 342. Liabilities of succeeding corporation.
  - (a) In general.
  - (b) Purchase at execution sale.
  - (c) Purchase at foreclosure or other judicial sale.
  - (d) Sale under the power in a deed of trust.
  - (e) Direct sale and transfer.
  - (f) Liability for torts.
  - (g) Special agreement to pay or assume debts and contracts.
  - (h) Implied assumption of debts or other liabilities.
  - (i) Transfers fraudulent as to creditors.
  - (j) Mere continuance of corporation.
  - (k) Liability imposed by statute.
  - (1) Obligations and covenants running with the property acquired.
- 343. Liability of the old corporation.
- 344. Change of state or other bank into a national bank.
  - (a) In general.
  - (b) Effect of change.
- 345. Reorganization agreements, and the rights of stockholders, bondholders, and creditors generally.
  - (a) Reorganization without foreclosure.
    - (1) In general.
    - (2) Effect of agreement and reorganization.
    - (3) Consideration for agreement.
  - (b) Transfer of property to a new corporation.

- (c) Foreclosure or sale under mortgage or deed of trust, and other judicial sales.
  - (1) In general.
  - (2) Rights as between bondholders.
  - (3) Rights of second mortgage bondholders.
  - (4) Who may purchase at foreclosure sale—ln general.
  - (5) Purchase and transfer by trustee.
  - (6) Purchase by or for stockholders.
  - (7) Purchase by directors or other officers.
  - (8) Rights of unsecured creditors.
  - (9) Payments or benefit to stockholders.
- (d) Construction of reorganization agreements.
- (e) Powers of reorganization committee-Notice.
- (f) Turning in bonds in payment for property.
- (g) Estoppel and laches.
- (h) Right to participate in reorganization.
- (i) Illegality in reorganization agreements.
- (j) Intention to create monopoly.
- (k) Rights and remedies against new corporation.
- (1) Liability to tax.
- (m) Statutory provision for reorganization.
  - (1) Power of the legislature.
  - (2) Implied assent of parties.
  - (3) Compliance with the terms and conditions of the statute.
  - (4) Reorganization independently of the statute.
- 346. Promotion of reorganizations.

#### II. CONSOLIDATION OF CORPORATIONS.

- § 347. In general.
  - 348. What constitutes a consolidation.
  - 349. Power to consolidate.
    - (a) Necessity for legislative authority.
    - (b) How authority is conferred.
    - (c) Ratification.
    - (d) Construction of statutes.
    - (e) Withdrawal or impairment of power.
    - (f) Dissent of stockholders.
    - (g) Dissent of creditors.
  - 350. Mode of effecting consolidation under legislative authority.
  - 351. Effect of unauthorized or ineffectual consolidation.
  - 352. De facto corporate existence.
  - 353. Estoppel to deny validity of consolidation.
  - 354. Dissolution of consolidating corporations, and creation of a new corporation.

- 355. Rights, powers, franchises, privileges, and property of the consolidated corporation.
  - (a) In general.
  - (b) Contracts and claims of the consolidating corporations.
  - (c) Subscriptions to stock.
  - (d) Municipal aid bonds and subscriptions.
  - (e) Exemptions from taxation.
  - (f) Effect of constitutional limitations and provisions.
  - (g) Effect of reservation of power to alter, amend, or repeal charters.
  - (h) Privilege or exemption enjoyed by one corporation only.
- 356. Burdens and liabilities of the consolidated corporation.
  - (a) In general.
  - (b) Liability on the contracts and for the debts of the consolidating corporations.
    - (1) In general.
    - (2) Statutory liability.
    - (3) Contract to exchange stock for bonds.
  - (c) Liability for the torts of the consolidating corporations.
  - (d) Consolidation after foreclosure sale.
  - (e) Continuance of the consolidating corporations.
  - (f) Taking renewal notes.
  - (g) Taking judgment against the old corporation,
  - (h) Remedy against the consolidated corporation.
    - (1) Action at law.
    - (2) Equity jurisdiction.
- 357. Rights of creditors against the consolidating corporations and their property.
- 358. Effect of consolidation with respect to liens.
- 359. Rights and liabilities of stockholders.
- 360. Authority of officers.
- 361. Effect of consolidation with respect to actions and proceedings.
- 362. Consolidation of corporations of different states.
  - (a) In general.
  - (b) Status of such a corporation in general.
  - (c) Citizenship and residence.
  - (d) Whether "incorporated under the laws" of a particular state.
  - (e) Conduct of business, meetings, contracts, etc.
  - (f) Control by the courts and by the legislature.
- 363. Remedies in the case of unauthorized or defective consolidations.

#### CHAPTER XIX.

#### MEMBERSHIP IN CORPORATIONS IN GENERAL.

- I. ACQUISITION OF MEMBERSHIP.
  - § 364. In general.
    - 365. Necessity for a contract.
    - 366. Joint-stock corporations.
    - 367. Corporations not having a capital stock.
    - 368. Power to admit or exclude members.
- II. Loss of Membership.
  - § 369. In general.
    - 370. Transfer of shares or membership.
    - 371. Forfeiture of shares or membership.
    - 372. Surrender of shares or withdrawal.
    - 373. Disfranchisement or expulsion of members.
      - (a) In general.
      - (b) Grounds for disfranchisement or expulsion.
      - (c) Mode of procedure.
      - (d) Remedies for wrongful expulsion.
      - (e) Review by the courts.

#### CHAPTER XX.

#### CAPITAL STOCK AND SHARES OF STOCK.

- I. NATURE OF CAPITAL STOCK AND SHARES OF STOCK.
  - § 374. In general.
    - 375. "Capital stock," "capital," "stock."
    - 376. Shares of stock.
      - (a) In general.
      - (b) As personal property,
      - (c) As "chattels," or "goods, wares, or merchandises."
      - (d) As "choses in action," "credits," "money," or "securities."
      - (e) Title as between husband and wife.
    - 377. Liability of stock to execution, attachment, garnishment, etc.
    - 378. Certificates of stock.
      - (a) Nature of certificate in general.
      - (b) Necessity for issue of certificates.
      - (c) As property.
      - (d) As choses in action, etc.

- (e) As negotiable instruments.
- (f) Issue of certificate as a transfer of stock.
- (g) Transfer of certificate as a transfer of stock.
- (h) Jurisdiction over certificate as jurisdiction over stock.
- (i) Matters elsewhere treated.
- 379. Conversion of shares of stock.
  - (a) In general.
  - (b) What constitutes a conversion.
  - (c) Measure of damages.
- II. ISSUE OF STOCK, AND PAYMENT THEREFOR.
  - § 380. In general.
    - 381. Power of corporations to create and issue stock.
    - 382. How stock may be issued.
    - 383. Payment for stock-In general.
    - 384. Payment in property, labor, or services.
      - (a) In general.
      - (b) Charter, statutory, or constitutional prohibitions.
      - (c) Ultra vires transactions.
    - 385. Payment in notes, bonds, and mortgages.
    - 386. Issue of stock in payment of a debt.
    - 387. Pledge of stock by the corporation.
    - 388. Right of stockholders to preference on issue of stock.
- III. WATERED OR FICTITIOUSLY PAID UP STOCK.
  - § 389. In general.
    - 390. Power of corporations in the absence of express charter, statutory, or constitutional provisions.
      - (a) Issue of stock for less than par.
      - (b) Issue of stock for property, labor, or services.
      - (c) Issue of stock gratuitously. '
      - (d) Issue of new stock on increasing capital stock.
      - (e) Stock issued and reacquired by the corporation.
      - (f) Payment by application of dividends or profits.
      - (g) Payment of commission to broker or agent.
    - 391. Special charter, statutory, or constitutional provisions.
    - 392. Valuation of property, labor, or services.
    - 393. Effect of issue of, or agreement to issue, watered stock.
    - 394. Effect as against the state.
    - 395. Effect as against the corporation itself.
    - 396. Effect as against the subscribers or purchasers.
    - 397. Effect as against dissenting stockholders.
    - 398. Effect as against stockholders participating, consenting, or acquiescing.
    - 399. Effect as against transferees.

- 400. Issue to directors or other officers.
- 401. Effect as against creditors.
  - (a) In general.
  - (b) Issue of stock for cash at a discount.
  - (c) Issue of stock for property, labor, or services.
  - (d) Issue of stock as a gratuity.
  - (e) Valuation of property.
  - (f) Loans to stockholders.
  - (g) Issue of additional stock after organization.
  - (h) Stock issued and reacquired by the corporation.
  - (i) Extent of liability.
  - (j) Existing creditors, and creditors participating, consenting, or with knowledge.
  - (k) Effect of transfer.
  - (1) Remedy of creditors.
- IV. Assessments upon Stockholders or Members after Payment in Full.
  - § 402. In general.
    - 403. Right to levy assessments.
    - 404. Power conferred by charter, statute, or agreement.
  - V. AMOUNT OF CAPITAL STOCK, AND INCREASE OR REDUCTION THEREOF.
    - § 405. In general.
      - 406. Amount of original capital stock.
      - 407. Increase and overissue of stock.
        - (a) In general.
        - (b) Grant of power by the legislature.
        - (c) Necessity for the increase.
        - (d) Ratification of unauthorized increase.
        - (e) Restriction or impairment of power.
        - (f) How and by whom the increase must be made or authorized.
        - (g) Effect of unauthorized increase or agreement there-
        - (h) Effect of informalities or irregularities.
        - (i) Subscriptions for the new stock.
        - (j) Estoppel as against creditors.
      - 408. Rights and remedies of existing stockholders with respect to the new stock.
      - 409. Sale of the new stock by the corporation.
      - 410. Liabilities arising out of increase of stock.
      - 411. Reduction of capital stock.
        - (a) In general.
        - (b) Reduction under legislative authority.
        - (c) Effect of reduction.
        - (d) Effect of purchase of shares by the corporation.

- 412. Increase or reduction in the number of shares, and of their par value.
- VI. PREFERRED OR GUARANTIED STOCK; INTEREST-BEARING STOCK; SPE-CIAL STOCK.
  - § 413. In general.
    - 414. "Preferred" or "guarantied" stock defined.
    - 415. Power to issue preferred or guarantied stock.
      - (a) In general.
      - (b) By-laws.
      - (c) Issue under power to borrow money.
      - (d) Extent of power.
      - (e) Remedies of stockholders.
    - 416. Effect of unauthorized issue or agreement to issue.
    - 417. Rights and remedies of preferred stockholders.
      - (a) In general.
      - (b) Change of contract or impairment of rights.
      - (c) Whether the relation is that of stockholders or creditors.
      - (d) Right to a certificate.
      - (e) Rights with respect to dividends.
      - (f) Rights as to management of corporation.
      - (g) Right to vote at corporate meetings.
      - (h) Rights on distribution of assets on insolvency or dissolution.
      - (i) Rights on increase or reduction of capital stock.
      - (j) Preferred stock convertible into bonds.
    - 418. Liabilities of preferred stockholders.
    - 419. Rights of common stockholders.
      - (a) In general.
      - (b) Exchange of common for preferred stock.
    - 420. Interest-bearing stock.
    - 421. Special stock under the Massachusetts statute.
- VII. BONDS, ETC., CONVERTIBLE INTO STOCK, AND STOCK CONVERTIBLE INTO BONDS, LAND, ETC.
  - § 422. In general.
- VIII. ISSUE AND CANCELLATION OF CERTIFICATES OF STOCK; LOST CERTIFICATES.
  - § 423. In general.
    - 424. Power to issue certificates, and validity of certificates.
    - 425. Right to certificates, and remedies for refusal to issue the same.
    - 426. Rights and remedies in case of loss of certificates.
    - 427. Cancellation of certificates.

- IX. RIGHTS AND LIABILITIES ARISING OUT OF THE ISSUE OF FICTITIOUS CERTIFICATES OF STOCK.
  - § 428. In general.
    - 429. Overissue of stock is void.
    - 430. Liability of corporation in damages.
    - 431. Authority of officer or agent issuing the certificate.
    - 432. Forged certificates.
    - 433. Certificates signed in blank.
    - 434. Stolen certificates.
    - 435. Persons who are entitled to relief.
    - 436. Remedies of the corporation.

#### CHAPTER XXI.

## SUBSCRIPTIONS TO CAPITAL STOCK, AND OTHER AGREEMENTS TO TAKE STOCK.

- I. NATURE AND FORMATION OF CONTRACTS OF SUBSCRIPTION AND OTHER AGREEMENTS.
  - § 437. In general.
    - 438. Subscriptions and other contracts defined and distinguished.
    - 439. Formation of contracts of subscription.
      - (a) In general.
      - (b) Subscriptions after corporation is formed.
      - (c) Subscriptions before corporation is formed.
      - (d) Formation of a different corporation.
    - 440. Consideration-Mutuality-Contracts under seal.
    - 441. Incomplete subscriptions.
    - 442. Subscription distinguished from agreement to subscribe.
    - 443. A subscription paper as an agreement between the subscribers.
    - Agreement to pay to agent or trustee for proposed corporation.
    - 445. Form of subscription and formalities in subscribing.
      - (a) In general.
      - (b) Form or formalities required by charter or statute.
      - (c) Necessity for writing-Statute of frauds.
      - (d) Requirement of formal articles of association,
      - (e) Signing subscription book.
      - (f) Acknowledgment of articles or agreement,
      - (g) Substantial compliance with charter or statute sufficient.
      - (h) Provisions which are merely directory.
    - 446. Subscription or agreement implied from conduct.

- 447. Effect of mistake.
- 448. Capacity of subscribers, and effect of disability.
  - (a) In general.
  - (b) Infants.
  - (c) Married women.
  - (d) Subscription by or for the corporation itself, and subscriptions by other corporations.
  - (e) Municipal corporations.
  - (f) Officers or agents of the corporation, and commissioners.
  - (g) Citizenship and residence.
- 449. Subscriptions made through agents and by partners.
  - (a) In general.
  - (b) Liability of pretended agent.
  - (c) Subscriptions by partners.
- 450. Authority and duties of persons receiving subscriptions.
  - (a) In general.
  - (b) Commissioners.
- 451. Revocation or withdrawal of subscriptions.
  - (a) Before formation of corporation or acceptance.
  - (b) After acceptance.
  - (c) Subscriptions under seal.
  - (d) Notice of revocation.
  - (e) Subscriptions irrevocable by force of charter or statute.
- 452. Lapse of subscriptions.
- 453. Illegality of subscriptions.
- 454. Proof of subscriptions.
- II. SUBSCRIPTIONS UPON EXPRESS CONDITIONS PRECEDENT; IMPLIED CONDITIONS PRECEDENT; CONDITIONAL DELIVERY.
  - § 455. In general.
    - 456. Conditional subscriptions defined.
    - 457. Distinguished from conditions upon special terms.
    - 458. Validity of conditions precedent.
      - (a) Subscriptions after the corporation is formed.
      - (b) Subscriptions before the corporation is formed.
    - 459. Effect of unauthorized conditional subscriptions.
    - 460. Oral conditions affecting written subscriptions.
    - 461. Effect of valid conditional subscriptions.
      - (a) Before performance or fulfillment of condition.
      - (b) After performance or fulfillment of condition.
      - (c) Construction and performance of conditions.
      - (d) Notice of performance.
    - 462. Implied conditions precedent.
      - (a) Fixing amount of the capital stock.

- (b) Subscription of the entire capital stock, or of a certain percentage thereof.
- (c) Payments on subscriptions.
- (d) Issue or tender of certificate of stock.
- (e) Formation of the corporation—Effect of irregularities and of failure to incorporate.
- 463. Waiver of conditions and estoppel.
- 464. Conditional delivery of subscriptions.

#### III. SUBSCRIPTIONS UPON SPECIAL TERMS.

- § 465. In general.
  - 466. Definition and effect.
  - 467. Power to accept subscriptions upon special terms, and validity thereof.
    - (a) In general.
    - (b) Violation of charter, statutory, or constitutional provisions.
    - (c) Special terms constituting a fraud upon other subscribers or creditors.
    - (d) Agreement to pay interest.
    - (e) Oral stipulations-Other writings.
    - (f) Authority of agents receiving subscriptions.

#### IV. FRAUD IN PROCURING SUBSCRIPTIONS.

- § 468. In general.
  - 469. Effect of fraud in general.
  - 470. Want of authority on the part of the person making the representation.
  - 471. What amounts to fraud in procuring subscriptions.
    - (a) In general.
    - (b) Nondisclosure or concealment of facts.
    - (c) Expression of opinion or prediction.
    - (d) Promises and statements of intention.
    - (e) Representations as to the law.
    - (f) Falsity of statement.
    - (g) Knowledge that the representation is false, and intent to deceive.
    - (h) The representation as an inducement.
    - (i) Right to rely on representations.
    - (j) Necessity for injury.
  - 472. Remedies of subscriber.
    - (a) Rescission in general.
    - (b) Recovery of money or other consideration.
    - (c) Action for deceit.
  - 473. Limitations upon the right to rescind.
    - (a) In general.

- (b) Ratification as a bar.
- (c) Return of stock.
- (d) Laches as a bar.
- (e) Removal of name from the books.
- (f) Rescission as against third persons.
- (g) Effect of insolvency of the corporation.

#### V. WITHDRAWAL, RELEASE, AND DISCHARGE OF SUBSCRIBERS.

- § 474. In general.
  - 475. Withdrawal.
  - 476. Release by corporation.
  - 477. Discharge by payment.
  - 478. Discharge by transfer.
  - 479. Discharge in bankruptcy.
  - 480. Discharge by alteration of contract.
  - 481. Discharge by nonperformance of conditions or special terms.
  - 482. Discharge by alteration or amendment of charter.
  - 483. Formation of a different corporation.
  - 484. Discharge by consolidation.
  - 485. Special agreements with, or release of, or nonpayment by, other stockholders.
  - 486. Exercise of powers granted by the charter or general law.
  - 487. Mismanagement of the corporation—Illegal election of officers, etc.
  - 488. Failure to comply with provisions of the charter or general law—Ultra vires acts.
  - 489. Nonuser or abandonment of enterprise.
  - 490. Delay in making calls—Statute of limitations.

#### VI. REMEDIES OF THE CORPORATION AGAINST SUBSCRIBERS.

- § 491. In general.
  - 492. Actions on subscriptions.
  - 493. Forfeiture or sale of shares.
  - 494. Effect of forfeiture or sale.
  - 495. Remedies in case of unauthorized or irregular forfeiture or sale.
  - 496. Set-off and counterclaim by subscribers.

#### VII. CALLS OR ASSESSMENTS ON UNPAID SUBSCRIPTIONS.

- § 497. In general.
  - 498. When calls are necessary.
  - 499. Validity and sufficiency of calls.
    - (a) In general.
    - (b) By whom made.
    - (c) Time of making calls-Conditions precedent.

- (d) Purpose of call, and necessity therefor.
- (e) Mode of making calls.
- (f) Inequality.
- (g) Partial invalidity.
- 500. Notice of calls, and demand of payment.
- VIII. ASSIGNMENT, MORTGAGE, OR PLEDGE OF UNPAID SUBSCRIPTIONS.
  - § 501. In general.
  - IX. INTEREST ON SUBSCRIPTIONS.
    - § 502. In general.
    - X. Subscription of Full Amount of the Capital Stock, or of a Specified Percentage Thereof.
      - § 503. In general.
        - 504. As a condition precedent to incorporation, or to commencement of business.
        - 505. As a condition precedent to liability on subscriptions.
        - 506. What subscriptions may be counted.
        - 507. Waiver and estoppel.
  - XI. PAYMENTS ON SUBSCRIPTIONS.
    - § 508. In general.
      - 509. Effect of nonpayment on legality of incorporation, or right to commence business.
      - 510. Effect of nonpayment on validity of subscriptions and liability of subscribers.
        - (a) In general.
        - (b) Failure to pay deposit at the time of subscribing.
      - 511. Sufficiency of payment.
  - XII. OVERSUBSCRIPTION AND APPORTIONMENT OR DISTRIBUTION OF STOCK.
    - § 512. In general.
      - 513. Effect of oversubscription.
      - 514. Distribution or apportionment by commissioners.
- XIII. ESTOPPEL OF SUBSCRIBERS.
  - § 515. In general.

#### CHAPTER XXII.

#### MISCELLANEOUS RIGHTS OF STOCKHOLDERS.

- I. THE RIGHT TO DIVIDENDS.
- § 516. Definition and nature of dividends.

- 517. Stockholders' right to share in profits.
  - (a) In general.
  - (b) Rights before dividend is declared.
  - (c) Rights after dividend is declared.
  - (d) Revocation of declaration.
  - (e) Effect of insolvency.
  - (f) Compelling declaration, and payment of dividends.
- 518. Right of corporation to pay dividends.
- 519. Dividends are payable out of profits only.
- 520. Determination of profits for the purpose of declaring dividends.
  - (a) In general.
  - (b) Property or money representing capital stock.
  - (c) Deduction of expenses and liabilities.
  - (d) Time of determining profits.
  - (e) Money due, but not received.
  - (f) Borrowed money.
  - (g) Creation of reserve fund for repairs, etc.
  - (h) Insurance companies.
  - Corporations whose property is necessarily consumed in use.
  - (j) Valuation of property.
- 521. Interest and interest dividends.
- 522. Set-off of dividends against debts due from stockholders.
- 523. Mode of declaring and paying dividends.
  - (a) In general.
  - (b) Mode of declaring dividends.
  - (c) Cash or property dividends.
  - (d) Bond or scrip dividends.
  - (e) Stock dividends.
  - (f) Discrimination between stockholders.
- 524. Time of payment.
- 525. Persons who are entitled to dividends.
  - (a) In general.
  - (b) All stockholders are entitled pro rata.
  - (c) Rights on transfer of stock.
    - (1) In general.
    - (2) Rights of pledgees.
    - (3) Transfers not made on the books of the corporation.
    - (4) Rights of legatees.
    - (5) Interpleader.
  - (d) Husband and wife.
  - (e) Other corporations.
- 526. Rights of persons entitled to the income or profits of shares.
  - (a) In general.
  - (b) Before declaration of a dividend.

- (c) After declaration of a dividend.
  - (1) Dividends declared before creation of the trust.
  - (2) Dividends declared after creation of the trust.
  - (3) Dividends declared out of capital.
  - (4) Proceeds of shares sold.
  - (5) Dividends in bonds or certificates of indebtedness.
  - (6) Right to subscribe for new shares, etc., and proceeds of a sale thereof.
  - (7) Stock dividends.
- (d) Rights on death of life beneficiary.
- 527. Remedies of stockholders to recover dividends.
  - (a) In general.
  - (b) Before a dividend has been declared.
  - (c) After a dividend has been declared.
    - (1) Action at law against the corporation.
    - (2) Action by transferee.
    - (3) Remedy in equity.
    - (4) Mandamus.
    - (5) Action against other stockholders.
    - (6), Action against officers of the corporation.
    - (7) Set-off of dividend against debt due to the corporation.
    - (8) Recovery of interest.
    - (9) Statute of limitations.
  - (d) Effect of consolidation.
- 528. Remedies for unlawful payment of dividends.
  - (a) In general.
  - (b) Recovery of dividends unlawfully paid.
    - (1) In general.
    - (2) Liability of transferee.
    - (3) Statute of limitations.
  - (c) Injunction.
  - (d) Bond or note given for illegal dividend.
  - (e) Liability of directors.
- 529. Rights of preferred stockholders.
  - (a) In general.
  - (b) The right to preference.
  - (c) Dividends payable out of profits only.
  - (d) Cumulative dividends.
  - (e) Discretion in declaring dividends.
  - (f) Stock and scrip dividends.
  - (g) Rights of transferees.
  - (h) Remedies of preferred stockholders.
- II. RIGHT TO INSPECT THE BOOKS AND PAPERS OF THE CORPORATION.
  - § 530. In general.

- 531. Express provisions in the charter, general law, articles of association, or by-laws.
- 532. Examination by attorney or agent.
- 533. Remedies of stockholders on denial of right.
- CONTRACTS AND CONVEYANCES BETWEEN A CORPORATION AND ITS STOCKHOLDERS.
  - § 534. In general.
- IV. ACTIONS BY STOCKHOLDERS TO ENFORCE INDIVIDUAL RIGHTS OR RE-DRESS OR PREVENT INDIVIDUAL INJURIES.
  - § 535. In general.
- V. Remedies of Stockholders for Injuries to the Corporation.
  - § 536. In general.
    - 537. Actions at law to redress injuries to the corporation.
    - 538. The general right of stockholders to sue in equity.
    - 539. Suits to enjoin or set aside ultra vires transactions, and prevent diversion or misapplication of assets.
    - Suits for redress or relief in case of fraud of the majority of stockholders.
    - 541. Suits for redress or relief in case of fraud, excess of authority, or negligence of directors or other officers.
    - 542. Suits against third persons to enjoin or redress injuries to the corporation.
    - 543. Necessity for effort to obtain relief through the corporation or its officers.
    - 544. Discretionary powers of the directors or majority of the stockholders.
      - (a) In general.
      - (b) Illustrations.
      - (c) Refusal to sue.
    - 545. Summary of the circumstances necessary to enable a stockholder to sue.
    - 546. Defense by stockholder in suits against the corporation.
    - 547. Suit or defense by a stockholder in the name of or for the corporation.
    - 548. Effect of assignment by the corporation.
    - 549. Effect of dissolution of the corporation.
    - 550. Suits by stockholders in the federal courts.
    - 551. Persons entitled to sue as stockholders.
    - 552. Motive of stockholder-Extent of interest.
    - 553. Laches and estoppel.
    - 554. Parties to stockholders' suits.
    - 555. Judgment or decree as a bar.
    - 556. Appointment of a receiver—Winding up or dissolution.

#### CHAPTER XXIII.

TRANSFER OF SHARES.
(For analysis in detail, see volume 3.)

#### CHAPTER XXIV.

MANAGEMENT OF CORPORATIONS. (For analysis in detail, see volume 3.)

#### CHAPTER XXV.

RIGHTS AND REMEDIES OF CREDITORS OF CORPORATIONS.

(For analysis in detail, see volume 3.)

#### CHAPTER XXVI.

FOREIGN CORPORATIONS. (For analysis in detail, see volume 3.)

TABLE OF CASES. (See volume 3.)

INDEX.
(See volume 3.)

### VOLUME II.

#### CHAPTER XVII.

#### DISSOLUTION OF CORPORATIONS.

- I. How Corporations may be Dissolved.
- § 302. In general.
  - 303. Constitutionality of dissolution.
  - 304. Dissolution by act of the legislature.
  - 305. Dissolution by expiration of time limited in charter.
  - 306. Dissolution by happening of prescribed contingency.
  - 307. Dissolution by failure or loss of integral part.
  - 308. Dissolution by surrender of charter.
  - 309. Suspension of business or nonuser of franchises.
  - 310. Alienation or loss of property and franchises.
  - 311. Insolvency—Appointment of receiver—Bankruptcy proceedings—Assignment.
- II. FORFEITURE OF CHARTER AND FRANCHISES IN JUDICIAL PROCEEDINGS BY THE STATE.
  - § 312. In general.
  - 313. Necessity for judicial proceedings and judgment of forfeiture.
  - 314. Grounds for forfeiture of charter.
    - (a) In general.
    - (b) Misuser or abuse of franchises in general.
    - (c) Nonuser of franchises, neglect of duty, etc.
    - (d) Breach of conditions subsequent.
    - (e) Inutility or impracticability of franchise or enterprise.
    - (f) Suspension or abandonment of business.
    - (g) Inability to continue business.
    - (h) Insolvency and failure to pay debts—Assignment for benefit of creditors.
    - (i) Alienation of property.
    - (j) Failure to hold meetings.
    - (k) Failure to keep or bring offices, officers, agencies, records, etc., within the state.
    - (1) Mere wrongful intent.
    - (m) Defective organization.
    - (n) Subsequent compliance with the law.
    - (o) Particular penalty prescribed by charter or by statute.
    - (p) Fine or judgment of ouster.
    - (q) Acts and neglects of officers as acts and neglects of corporation.
    - (r) Acts of stockholders as acts of corporation.

- 315. Waiver of forfeiture and estoppel of the state.
  - (a) In general.
  - (b) In case of dissolution, ipso facto, on failure to comply with conditions.
  - (c) Implied waiver.
  - (d) Mere acquiescence and lapse of time.
  - (e) Continuing cause of forfeiture.
  - (f) Knowledge of cause of forfeiture.
  - (g) Who may waive a forfeiture.
  - (h) Conditional waiver.
  - (i) Violation of contract by the state.

#### III. PROCEDURE AND JURISDICTION.

- § 316. In general.
  - 317. Mode of procedure at common law.
  - 318. By what authority proceedings must be instituted.
  - 319. Jurisdiction of courts of equity.
  - 320. Statutory jurisdiction.
  - 321. Jurisdiction over foreign corporations.

#### IV. EFFECT OF DISSOLUTION.

- § 322. In general.
  - 323. Dissolution may be set up collaterally.
  - 324. When dissolution takes effect.
  - 325. Effect of dissolution with respect to franchises.
  - 326. Effect of dissolution with respect to debts and contracts.
  - 327. Effect of dissolution with respect to torts.
  - 328. Effect of dissolution with respect to property and conveyances.
  - 329. Effect of dissolution with respect to actions and proceedings.
  - 330. Effect of dissolution on transfer of stock.
- V. CONTINUANCE AND WINDING UP OF CORPORATIONS UNDER STATUTORY PROVISIONS.
  - § 331. In general.
    - 332. Continuance of existence of corporations.
      - (a) In general.
      - (b) Collection of debts.
      - (c) Engaging in new business.
      - (d) Power to hold property.
      - (e) Disposal of property.
      - (f) Liability for torts.
      - (g) Actions and proceedings.
      - (h) Effect of statute on equity jurisdiction.
    - 333. Officers as trustees for creditors and stockholders.
    - 334. Appointment of receiver or trustee.
      - (a) In general.
      - (b) Appointment of successor.
      - (c) Appointment by governor or legislature.
      - (d) Where a trustee or receiver has been appointed by or with consent of corporation.

- (e) Where directors or other officers are made trustees.
- (f) Where existence of corporation is continued by statute.
- (g) Time of application or appointment.
- (h) Who may apply for a receiver.
- (i) Who may be appointed receiver.
- (j) Order appointing receiver.
- (k) Effect of appointment of receiver.
- (1) Transfer of property.
- (m) Powers and duties of receivers.
- (n) Temporary receiver.

#### I. How Corporations may be Dissolved.

- § 302. In general.—In the absence of statutory provisions, a corporation may be dissolved, and thus cease to exist, in the following ways only:
- (1) By an act of the legislature repealing or withdrawing its charter, provided the legislature, in granting the charter, has reserved the power to repeal the same, but not otherwise.
  - (2) By the expiration of a time limited in its charter.
- (3) By the happening of some contingency prescribed in its charter.
- (4) By the failure or loss of some integral part of the corporation, without which it cannot exist.
- (5) By a surrender of its charter, authorized or accepted by the state.
- (6) By the forfeiture of its charter in a judicial proceeding by the state for misuser, or nonuser, or failure to perform conditions subsequent.

Other modes of dissolution are provided for by statute in most jurisdictions.

The dissolution of a corporation is not unconstitutional as impairing the obligation of contracts between the corporation and its creditors.

A corporation is said to be dissolved when the franchise to be a corporation conferred upon it by the state is extinguished, and its corporate existence terminated.<sup>1</sup> It is said by Blackstone that a corporation may be dissolved in four ways, namely:

1 "The dissolution of a corpora- and extinguishment of all the tion is that condition of law and legal relations subsisting in refact which ends the capacity of spect of the corporate enterprise." the body corporate to act as such, Taylor, Corp. § 428. and necessitates a final liquidation

(1) By act of parliament; (2) by the natural death of all its members, in case of an aggregate corporation; (3) by the surrender of its franchises into the hands of the king, which he calls a kind of suicide; and, (4) by forfeiture of its charter through negligence or abuse of its franchises: in which case. he says, the law judges that the body politic has broken the condition upon which it was incorporated, and thereupon the incorporation is void.<sup>2</sup> This statement, however, is not accurate when applied to modern business corporations in this country. As we shall presently see, the legislature cannot repeal the charter of a corporation unless the power to do so was reserved when the corporation was created.<sup>3</sup> Nor can modern joint-stock companies be dissolved by the death of members, for the shares of stock in such corporations pass, on the death of the holders, to their personal representatives or legatees.4 Nor, according to the weight of authority, can a corporation be dissolved by the surrender of its charter, unless the surrender is authorized or accepted by the state.<sup>5</sup> Nor does a corporation cease to exist, ipso facto, because of negligence or abuse of its franchises. There must first be a judgment of forfeiture in proceedings by the state.6

It is more accurate, therefore, to say that a corporation may be dissolved in the following ways: (1) By an act of the legislature repealing or withdrawing its charter, provided the legislature, in granting the charter, has reserved the power to repeal the same, but not otherwise; (2) by the expiration of a time limited in its charter for the continuance of its corporate existence; (3) by the happening of some contingency prescribed in its charter; (4) by the failure or loss of some integral part of the corporation, so that it cannot longer exist;

<sup>21</sup> Bl. Com. 485. And see 2 Kyd, Corp. 447; 2 Kent's Com. 245; Angell & Ames, Corp. 501; Oakes v. Hill, 14 Pick. (Mass.) 442; Biston Glass Manufactory v. Langdon, 24 Pick. (Mass.) 49, 35 Am. Dec. 292, 2 Smith's Cas. 604, 1 Cum. Cas. 478; Penobscot. Boom

Corp. v. Lamson, 16 Me. 224, 33 Am. Dec. 656; Hodsdon v. Copeland, 16 Me. 314.

<sup>3</sup> Post, § 304.

<sup>4</sup> Post, § 307.

<sup>&</sup>lt;sup>5</sup> Post, § 308.

<sup>6</sup> Post, § 313.

(5) by a surrender of its charter, provided the surrender is authorized or accepted by the state; and (6) by the forfeiture of its charter in a judicial proceeding by the state.

## § 303. Constitutionality of dissolution.

The dissolution of a corporation is not unconstitutional as impairing the obligation of contracts made by it with other parties during its existence, for they may still assert their rights against the property of the corporation in the mode. if any, prescribed by statute, or, if no adequate remedy is provided by statute, in a court of chancery in accordance with the general principles and practice in equity. This is true, whether the dissolution be by repeal of the charter of a corporation under a power of repeal reserved in granting it, or by a surrender of the charter by the stockholders or members, authorized or accepted by the state, or by a forfeiture of its charter in judicial proceedings by the state.7 Furthermore, "a corporation, by the very terms and nature of its political existence, is subject to dissolution, by a surrender of its corporate franchises, and by a forfeiture of them for willful misuser and nonuser. Every creditor must be presumed to understand the nature and incidents of such a body politic, and to contract with reference to them. And it would be a doctrine new in the law, that the existence of a private contract of the corporation should force upon it a perpetuity of existence contrary to public policy, and the nature and objects of its charter." 8

It must be borne in mind, however, that, while the legisla-

Cas. 618, 1 Cum. Cas. 468; Foster Ala. 573; Nelson v. Hubbard, 96 v. Essex Bank, 16 Mass. 245, 8 Ala. 238.

Am. Dec. 135, 2 Smith's Cas. 608, 8 Mr. Justice Story, in Mumma 1 Cum. Cas. 464; Read v. Frankfort Bank, 23 Me. 318, 2 Smith's 2 Smith's Cas. 614, 1 Cum. Cas. Cas. 707; Curran v. State, 15 How. 459.

<sup>7</sup> Mumma v. Potomac Co., 8 Pet. (U. S.) 310; Lum v. Robertson, 6 (U. S.) 281, 2 Smith's Cas. 614, 1 Wall. (U. S.) 277; Lothrop v. Cum. Cas. 459; Thornton v. Marstedman, 13 Blatchf. 134, Fed. ginal Freight Ry. Co., 123 Mass. 32, Cas. No. 8,519; Merrill v. Suffolk 1 Cum. Cas. 462; Bacon v. Robertson, 18 How. (U. S.) 480, 2 Smith's Mobile & Ohio R. Co. v. State, 29

ture may provide for the dissolution of a corporation, whether it is indebted or not, it cannot impair the obligation of the existing contracts between it and third persons, or take away the vested rights of its creditors. It cannot constitutionally pass any law which deprives creditors of the right to resort to the property of the corporation for the satisfaction of their claims.

And, of course, a repeal of the charter of a corporation, except for some act or neglect constituting a cause for forfeiture of its charter, is void as impairing the obligation of the contract between the state and the corporation, unless the corporation consents, or the power to repeal has been reserved by the state.<sup>10</sup>

### § 304. Dissolution of corporation by act of the legislature.

(a) In general.—Unless prevented by constitutional prohibitions, a corporation may be dissolved by an act of the legislature repealing its charter. The absolute repeal of a charter. when the repeal is within the power of the legislature, dissolves the corporation, in the absence of provision to the contrary, and it cannot afterwards exercise any corporate power. was said by Mr. Justice Miller in a leading case in the supreme court of the United States: "One obvious effect of the repeal of a statute is that it no longer exists. Its life is at an end. Whatever force the law may give to transactions into which the corporation entered and which were authorized by the charter while in force, it can originate no new transactions dependent on the power conferred by the charter. If the corporation be a bank, with power to lend money and to issue circulating notes, it can make no new loan nor issue any new notes designed to circulate as money. If the essence of the grant of the charter be to operate a railroad, and to use the streets of the city for that purpose, it can no longer so use the streets of the city, and no longer exercise the franchise of

People v. O'Brien, 45 Hun (N. Rep. 684, 2 Smith's Cas. 728;
 Y.) 519, 111 N. Y. 1, 7 Am. St. Lothrop v. Stedman, 42 Conn. 584.
 10 Ante § 270 et seq.

running a railroad in the city. In short, whatever power is dependent solely upon the grant of the charter, and which could not be exercised by unincorporated private persons under the general laws of the state, is abrogated by repeal of the law which granted these special rights." 11

The repeal of a charter, however, does not destroy property and contract rights acquired by the corporation before the repeal. "Personal and real property acquired by the corporation during its lawful existence, rights of contract, or choses in action so acquired, and which do not in their nature depend upon the general powers conferred by the charter, are not destroyed by such a repeal; and the courts may, if the legislature does not provide some special remedy, enforce such rights by the means within their power. The rights of the shareholders of such a corporation, to their interest in its property, are not annihilated by such a repeal, and there must remain in the courts the power to protect those rights."12

(b) Power of legislature to repeal a charter.—As was shown at some length in another chapter, the charter of a private corporation is a contract between the corporation and the state, within the meaning of the prohibition in the constitution of the United States against the passage by a state of any law impairing the obligation of contracts, and therefore, when a state has granted a charter to a corporation, without reserving the right to repeal the same, it cannot constitutionally repeal the same and dissolve the corporation, without its consent, before expiration of the time for which it was created, 13 unless, as will be explained in another section, the corporation has done something not authorized by its charter, or left undone

<sup>&</sup>lt;sup>11</sup> Greenwood v. Union Freight <sup>12</sup> Mr. Justice Miller, in Green-R. Co., 105 U. S. 13, 2 Smith's Cas. wood v. Union Freight R. Co., 105 720, 1 Cum. Cas. 538. See, also, U. S. 13, 2 Smith's Cas. 720, 1 People v. O'Brien, 45 Hun (N. Y.) Cum. Cas. 538. And see People v. 519, 111 N. Y. 1, 7 Am. St. Rep. O'Brien, 45 Hun (N. Y.) 519, 111 684, 2 Smith's Cas. 728; International & Great Northern Ry. Co. Smith's Cas. 728. See post, §§ v. State, 75 Tex. 356; Read v. Frankfort Bank, 23 Me. 318, 2 Smith's Cas. 707.

<sup>326, 327.</sup> 

<sup>13</sup> See ante, § 270 et seq.

something required of it, and thereby forfeited its right to continue in the exercise of its franchises.14

Of course the legislature may repeal the charter of a corporation at any time with the consent of the stockholders or members.15 And if the state, in granting a charter, has reserved the right to repeal the same, either by a provision to that effect in the charter itself, or by a constitutional provision or general law in force at the time of the grant, the reservation enters into the contract between the state and the corporation. If the power to repeal the charter at the will or pleasure of the legislature is reserved, the power to repeal the same is absolute, and may be exercised at any time, and without any cause of forfeiture, provided vested rights are not impaired.<sup>16</sup> If the power has been reserved to repeal the charter of a corporation only on the happening of a certain contingency, the happening of such contingency is a condition precedent to the power to repeal the same and dissolve the corporation. the power is absolute upon the happening of such contingency. 17

As we have seen in another chapter, some of the courts have held that where the legislature has reserved the right to repeal a charter in case of misuser or nonuser of its franchises by the corporation, the legislature has the power to determine whether there has been nonuser or misuser, without any judicial proceeding to determine the question, and, further than this, that its action in the matter is not subject to review by the courts. 18

14 See post, § 312 et seq. 29 Ala. 573; post, § 308.

the corporation cannot object. See

supra, § 303.

Ry. Co., 123 Mass. 32, 1 Cum. Cas. 462; Greenwood v. Union Freight R. Co., 105 U. S. 13, 2 Smith's Cas. 720, 1 Cum. Cas. 538; Com. v. Bońsall, 3 Whart. (Pa.) 559; Read v. Frankfort Bank, 23 Me. 318, 2

Grant's Cas. (Pa.) 274, 26 Pa. St. 15 Mobile & Ohio R. Co. v. State, 287, 2 Smith's Cas. 710; Com. v. As we have seen, creditors of e corporation cannot object. See tyra, § 303.

16 Thornton v. Marginal Freight y. Co., 123 Mass. 32, 1 Cum. Cas. 267, 2 Shith S Cas. 710; Com. v. Pittsburgh & Connellsville R. Co., 58 Pa. St. 26; Flint & Fentonville Plank Road Co. v. Woodhull, 25 Mich. 99, 12 Am. Rep. 233; State v. Noyes, 47 Me. 189; Chesapeake & Ohio Canal Co. v. Baltimore & Ohio R. Co., 4 Gill & J. (Md.) 1,

18 Miners' Bank of Dubuque v. United States, 1 G. Greene (Iowa) 553, Morris (Iowa) 482, 43 Am. Smith's Cas. 707. Dec. 115./ See, also, Mobile & 17 Crease v. Babcock, 23 Pick. Ohio R. Co. v. State, 29 Ala. 573; (Mass.) 334, 34 Am. Dec. 61; Erie Farnsworth v. Minnesota & Pa-& North East R. Co. v. Casey, 1cific R. Co., 92 U. S. 49.

Other courts have held that such a reservation of the right to repeal a charter contemplates judicial proceedings for the purpose of determining whether there has been nonuser or misuser on the part of the corporation, and that the legislature cannot determine the question itself and repeal the charter without such proceedings.19 Other courts have held that the legislature may determine the question in the first instance, and repeal the charter, but that its determination is reviewable by the courts.20

The right reserved to the legislature in the charter of a corporation, to repeal it for abuse, is not affected by judicial proceedings to restrain such abuse, nor is it defeated by a discontinuance of the abuse.21

(c) What constitutes the repeal of a charter.—In the absence of constitutional restrictions, a special charter, or the charter of a corporation organized under a general law, may be repealed either by a special act or by a general law. Whether an act operates as a repeal, assuming that the power to repeal exists, depends, of course, upon the intention of the legislature. The repeal of a charter, like the repeal of any other statute, may be express or implied, though implied repeals are not favored.

"There is no rule of law," it was said in a New Jersey case, "which prohibits the repeal of a special charter by a general law. Nor is there any principle of law forbidding such repeal,

<sup>19</sup> State v. Noyes, 47 Me. 189; Flint & Fentonville Plank Road Co. v. Woodhull, 25 Mich. 99, 12 Am. Rep. 233; Chesapeake & Ohio Canal Co. v. Baltimore & Ohio R. Co., 4 Gill & J. (Md.) 1, 122. See, also, Shand v. Gage, 9 S. C. 187.

Where the legislature has repealed a private act of incorporation without a judicial determination, as required by a provision of the act, of the question whether there had been a violation of any of the charter provisions, the repealing act cannot be sustained Casey, 26 Pa. St. 287, 1 Grant's subject to a right in the corpora-Cas. 274.

tors to have the question of violation tried in the courts afterwards, since an act, if valid for any purpose, must be conclusive. Flint & Fentonville Plank Road Co. v. Woodhull, 25 Mich. 99, 12 Am. Rep. 233.

20 Erie & North East R. Co. v. Casey, 1 Grant's Cas. (Pa.) 274, 26 Pa. St. 287, 2 Smith's Cas. 710; Com. v. Pittsburgh & Connellsville R. Co., 58 Pa. St. 26.

without the use of express words declarative of the legislative intent to repeal the earlier statute. Repeals by implication are not favored. But the question is always one of legislative intent, and the intent to abrogate the particular enactment in an earlier statute by a general enactment in a later statute, is sufficiently manifested where the provisions of the two enactments are so inconsistent that they cannot stand together."22

As stated above, however, repeals by implication are not favored, and a statute should not be construed as impliedly repealing the charter of a corporation, if it reasonably admits of any other construction.<sup>23</sup> It has been held, therefore, that the repeal of a general law authorizing the formation of corporations will not be construed as a repeal of the charters of corporations which have been formed under it, unless such an intention on the part of the legislature appears either from the express terms of the repealing statute or by necessary implication.24

A constitutional provision abolishing all monopoly features in the charter of any corporation existing in the state does not entirely annul the charter of a corporation which has been given a monopoly, but merely abolishes the monopoly feature thereof.25

22 Morris & Essex R. Co. v. 300; Freehold Mutual Loan Ass'n Commissioner of Railroad Taxa-tion, 37 N. J. Law, 228, 230. See pare, however, Wilson v. Tesson, also, Mechanics' & Traders' Bank 12 Ind. 285; Cooper v. Arctic of Jersey City v. Bridges, 30 N. J. Ditchers, 56 Ind. 233. See, also, Law, 112; Union Improvement Co. ante, § 281. v. Com., 69 Pa. St. 140. Compare, however, City of Grand Rapids v. general law is not dissolved by a Grand Rapids Hydraulic Co., 66 repeal thereof, where the repeal-Mich. 606.

23 Mechanics' & Traders' Bank of Jersey City v. Bridges, 30 N. J. Law, 112; Morris & Essex R. Co. v. Commissioner of Railroad Taxation, 37 N. J. Law, 228; Bibb v. baugh, 5 Iowa, 300.

Ass'n v. Benshimol, 130 Mass. 325; of any corporation existing in the

A corporation organized under a ing act contains a proviso saving rights acquired in proceedings had under existing laws. Barren Creek Ditching Co. v. Beck, 99 Ind. 247.

25 Putnam v. Ruch, 54 Fed. 216, Hall, 101 Ala. 79; United Hebrew 56 Fed. 416, where it was held Benevolent Ass'n v. Benshimol, that the adoption in Louisiana of 130 Mass. 325; Donworth v. Cool- a constitutional provision regulating the slaughter of cattle, and 24 United Hebrew Benevolent abolishing all monopoly features Donworth v. Coolbaugh, 5 Iowa, state, did not entirely annul the

#### § 305. Dissolution of corporation by expiration of time limited in its charter.

Another mode in which a corporation may be dissolved is by the expiration of a time limited in its charter for the continuance of its corporate existence. As was explained in another chapter, a corporation has the capacity of perpetual succession, and there have been many instances in which corporations have been created to exist forever. At present, however, they are seldom given so long life. The legislature may, and generally does, limit their existence to a certain number of years.26

When the time during which a corporation is to exist is thus limited by its charter, it is dissolved and ceases to exist upon the expiration of the time limited, and its existence as a corporation cannot be continued after that time, except by legislative authority, even with the consent of all the stockholders or members.27 According to the better opinion, as was shown in another chapter, a body of men has not even a de facto corporate existence after expiration of the time for which its corporate existence is limited by its charter.28

New Orleans.

pacity of perpetual Snell v. City of Chicago, 133 Ill.

25 Fed. 882; Commercial Bank v. (Va.) 56, 40 Am, Dec. 726; Rider Lockwood's Adm'r, 2 Har. (Del.) v. Nelson & Albemarle Union Fac-8; Atlantic & Gulf R. Co. v. Allen, tory, 7 Leigh (Va.) 156, 30 Am. 15 Fla. 637; Marysville Investment Co. v. Munson, 44 Kan. 491; Bank of Galliopolis v. Trimble, 6 Va. 605. B. Mon. (Ky.) 601; Grand Rapids
Bridge Co. v. Prange, 35 Mich. 400,
545, 54 Am. St. Rep. 685; Krutz v.
24 Am. Rep. 485; Bank of Mississippi v. Wrenn, 3 Smedes & M.
preme Lodge, Knights of Pythias,
(Miss.) 791; Bradley v. Reppell,
v. Weller, 93 Va. 605; Dobson v.

charter of a corporation which 133 Mo. 545, 54 Am. St. Rep. 685; had been given the exclusive right People v. Walker 17 N. Y. 502; to slaughter cattle in the city of Sturges v. Vanderbilt, 73 N. Y. 384; ew Orleans. Sturgis v. Drew, 11 Hun (N. Y.) <sup>26</sup> When a corporation is created 136; Asheville Division No. 15, by a special act without any limit- Sons of Temperance, v. Aston, 92 ation as to the duration of exist-N. C. 578; Dobson v. Simonton, ence, its charter gives it the ca-86 N. C. 492; La Grange & Memexistence. phis R. Co. v. Rainey, 7 Cold. (Tenn.) 420; Steadman v. Mer-413; State v. Ladies of the Sacred chants' & Planters' Bank of Sher-Heart, 99 Mo. 533; note 29, infra. man, 69 Tex. 50; May v. State <sup>27</sup> Mason v. Pewabic Mining Co., Bank of North Carolina, 2 Rob. 495; Supreme Knights of Pythias, v. Weller, 93

Duration.—Whether the charter of a corporation, or the general law under which it is organized, or its articles of incorporation, as the case may be, gives it the right to exist forever, or limits its existence to a certain period, and, in the latter case, the period to which it is limited, depends, of course, upon the language of the particular statute or articles. Some of the decisions construing particular statutes or articles are referred to in the note below.<sup>29</sup> In some states the constitution prohibits the creation of corporations, with certain excep-

29 Where she charter of a corporation provides that its existence shall continue "until" a speci-

"perpetual succession" gives it the right to exist forever, unless there is something to show that the legislature used the words in a different sense. Fairchild v. Masonic Hall Ass'n, 71 Mo. 526; Snell v. City of Chicago, 133 Ill. 413. And see State v. Ladies of the Sacred Heart, 99 Mo. 533. Compare Scanlan v. Crawshaw, 5 Mo. App. 337.

The use of the words "perpetual succession," however, does not necessarily imply continuance forever, and if it appears that the legislature intended them in sense of continuity for a particular time, they must be so limited. In a late Missouri case, an act incorporating a gas light company provided that it should have "perpetual succession," and that it should have the exclusive right to manufacture gas and coke in a certain city for thirty years, and repealed all acts inconsistent therewith. At the time the act was passed, a general law was in force,

Simonton, 86 N. C. 492; and other limitation, for twenty years. It cases in the note preceding. See, also, ante, § 82(c)(4). was not inconsistent with the special act, and that the corporation was created for thirty years only, the words "perpetual succession" fied day, the charter expires at being intended merely to give the the end of the preceding day. People v. Walker, 17 N. Y. 502. it continued in existence, and not A provision in the charter of a to define its duration. In this corporation that it shall have case, the court was influenced by the fact that the policy of the state of Missouri, as shown by its general legislation, was unfavorable to the unlimited duration of purely private corporations, and said that all doubts as to the intention of the legislature should be resolved against an intention to grant perpetual existence. State v. Payne, 129 Mo. 468.

A statute providing that every corporation shall have succession by its corporate name for the period limited in its charter, and, when no period is limited, for ten years, has no application to a subsequent charter, in which it is provided that the corporation shall have perpetual succession forever. and the period of its existence is not limited. State v. Stormont. 24 Kan. 686.

Where a corporation formed under an act authorizing corporations to exist for five years only was revived for limited periods by subsequent acts, and finally by an act putting no limit to its duradeclaring that every corporation tion, it was held that it was no should have capacity of succession longer subject to the five-year for the period limited in its char-limitation, but was entitled to exist ter, and, if there should be no until repeal of the last act. Vantions, for a longer period than a certain number of years.<sup>30</sup> And in some it is expressly provided, either by the constitution or by a general law, that succession by a corporate name shall be limited to a certain number of years, when no period is fixed by its charter.<sup>31</sup> In the absence of such a provision in the constitution or general law, the creation of a corporation without any limitation as to the period of its existence entitles it to perpetual existence.<sup>32</sup>

derbilt v. Eagle Iron Works, 25 Wend. (N. Y.) 665.

The duration of a corporation is not limited by a provision in its charter that it shall be void if not carried into effect within a specified time, nor by a provision that the state may purchase its entire property after a certain number of years. City of Roxbury v. Boston & Providence R. Corp., 6 Cush. (Mass.) 424.

Where the cha 'er of a corporation limits its existence to fifty years, but by an amendatory act it is provided that, at the expiration of each subsequent term of ten years, the state shall have the right, at its election, to take all the property of the company at the par value of its stock, and, if this election is not made within twelve months, then the charter of the company shall be continued for another term of ten years, the corporation has the capacity of perpetual succession, unless the election to purchase is exercised by the state. Davis v. Memphis & Charleston R. Co., 87 Ala. 633.

Where the duration of a corporation was limited to thirty years by its articles, in accordance with and providing for the statute under which it was organized, and afterwards purchasers of its property and franchises were incorporated by an act which provided that they should have "perpetual succession," but which declared that they should be "subject to like restrictions in all respects" as if incorporated under the law under provision for his provision for his and providing for manent endowm lishes a perpetual, each provision for his and providing for manent endowm state v. Lesueur, Clowes, 3 N. Y. 47 of the Sacred H vanderbilt v. Extremely should be "subject to like restrictions in all respects" as if incorporated under the law under

which the first-mentioned corporation was formed, it was held that the charter of the corporation expired in thirty years from its date. State v. Hannibal & Ralls County Gravel Road Co., 138 Mo. 332.

36 In Michigan it has been held that the constitutional provision that "no corporation except for municipal purposes, or for the construction of railroads, plank roads, and canals, shall be created for a longer time than thirty years," was only intended to apply to corporations of a private nature, organized for profit and the accumulation of wealth, and does not apply to those of a public character, designed solely for the purpose of education and improvement. And it was held, therefore, that it did not apply to county agricultural societies. Kent County Agricultural Society v. Houseman, 81 Mich. 609.

31 Articles of incorporation of an institution placing the management in a board of trustees, declaring that "the trusteeship shall be perpetual, each trustee making provision for his own successor," and providing for the use of permanent endowment funds, establishes a perpetual corporation. State v. Lesueur, 141 Mo. 29.

32 Farmers' Loan & Trust Co. v. Clowes, 3 N. Y. 470; State v. Ladies of the Sacred Heart, 99 Mo. 533; Vanderbilt v. Eagle Iron Works, 25 Wend. (N. Y.) 665; East Tennessee Iron Mfg. Co. v. Gaskell, 2 Lea (Tenn.) 742.

Where a general law authorizing the formation of corporations limits the period for which they may exist to a certain number of years, the articles of incorporation cannot extend the existence of a corporation organized under the law beyond such period. But if the articles do undertake to provide for a longer period of existence than the law allows, they are not void. The excess may be rejected as surplusage, and the incorporation is valid for the authorized period.33

Continuance for purpose of winding up.—Sometimes, by express statutory enactment, the existence of corporations created for a limited time are extended for a certain time beyond the period limited, for the purpose of winding up their affairs, and of allowing suits by and against them.<sup>34</sup> Such a statute, as we have seen, may be constitutionally enacted after a corporation is created for a limited time, for it does not impair any rights of the corporation, or of its creditors or stockholders, but merely provides for the enforcement of rights which, in the absence of a statute, would be recognized and enforced in equity.35

# § 306. Dissolution of corporation by the happening of a contingency prescribed by its charter.

A corporation may also be dissolved by the happening of some contingency prescribed in its charter, without any further act upon the part of the legislature, and without any judicial proceedings to declare a forfeiture. If the legislature clearly provides in the charter of a corporation that it shall cease to exist on the happening of a certain contingency, the happening of such contingency ipso facto terminates the charter and dissolves the corporation. No act of the legislature or judgment of a court declaring a forfeiture is necessary.36

<sup>33</sup> People v. Cheeseman, 7 Colo. 376. See ante, § 76.

<sup>2</sup> Woods, 186, Fed. Cas. No. 12,246;
34 See post, § 332.
36 Foster v. Essex Bank, 16 Mass.
245, 8 Am. Dec. 135, 2 Smith's
13 Am. Rep. 181, 1 Smith's Cas.
Cas. 608, 1 Cum. Cas. 464; ante,
§ 303.
2 Woods, 186, Fed. Cas. No. 12,246;
Oakland R. Co. v. Oakland, Brooklyn & F. V. R. Co., 45 Cal. 365,
13 Am. Rep. 181, 1 Smith's Cas.
Cas. 608, 1 Cum. Cas. 464; ante,
§ 303.

<sup>36</sup> Sala v. City of New Orleans. 2 Woods, 188, Fed. Cas. No. 12,246;

It was so held in a New York case, where the charter of a railroad company provided that, unless the company should be organized and at least one mile of road built within three years, the charter and all the powers, rights, and franchises therein and thereby granted should "be deemed forfeited and terminated." . The court said in this case: "The general principle is not disputed that a corporation, by omitting to perform a duty imposed by its charter or to comply with its provisions does not ipso facto lose its corporate character or cease to be a corporation, but simply exposes itself to the hazard of being deprived of its corporate character and franchises by the judgment of the court in an action instituted for that purpose by the attorney general in behalf of the people; but it cannot be denied that the legislature has the power to provide that a corporation may lose its corporate existence without the intervention of the courts by any omission of duty or violation of its charter or default as to limitations imposed, and whether the legislature has intended so to provide in any case depends upon the construction of the language used. Here the language used shows that the legislature intended to make the continued existence of the plaintiff as a corporation depend upon its compliance with the requirements of section seventeen of the original act. In case of noncompliance the act itself was to cease to have any operation, and all the powers, rights and franchises thereby granted were to be 'deemed forfeited and terminated.'

529; Peavey v. Calais R. Co., 30 Orange & C. R. Co., 27 Grat. (Va.) Me. 498; Dane v. Young, 61 Me. 160; Ford v. Kansas City & Independence Short Line R. Co., 52 lyn, 78 N. Y. 524, 1 Smith's Cas. 365; In re Brooklyn, Winfield & Newtown R. Co., 75 N. Y. 335, 81 N. Y. 69; Sturges v. Vanderbilt, 73 N. Y. 384; In re Brooklyn, Winfield & Newtown Ry. Co., 72 N. Y. 245; Com. v. Lykens Water Co., 110 Pa.

119.

Where an act of incorporation Mo. App. 439; In re Public Highway, 22 N. J. Law, 293; Brooklyn tain amount of capital stock, and Steam Transit Co. v. City of Brookthat there should be a cerway, 22 N. J. Law, 293; Brooklyn tain amount of capital stock, and that subscriptions should be paid in full before the commencement of business, and declared that the act should be void unless the corporation should organize and commence business within two years, it was held that failure to subscribe and pay in the capital stock St. 391; City of Houston v. Hous- within two years forfeited the ton Belt & M. P. Ry. Co., 84 Tex. charter. People v. National Sav-581; Silliman v. Fredericksburg, ings Bank, 129 Ill. 618.

There was to be not merely a cause of forfeiture which could be enforced in an action instituted by the attorney general, but the powers, rights and franchises were to be taken and treated as forfeited and terminated. At the end of the time limited the corporation was to come to an end, as if that were the time limited in its charter for its corporate existence."37

As we shall see, however, in a subsequent section, while it is within the power of the legislature to thus provide that the existence of a corporation shall cease, without any judicial proceedings and judgment of forfeiture, upon its failure to comply with certain conditions, such an intention on the part of the legislature should not be implied from language which will reasonably admit of a different construction. "It requires, however, strong and unmistakable language, thorize the court to hold that it was the intention of the legislature to dispense with judicial proceedings on the intervention of the attorney general."38

#### § 307. Dissolution of corporation by failure or loss of an integral part.

Another way in which a corporation may be dissolved, without any action on the part of the legislature or courts, is by the failure or loss of some integral part of its organization which is necessary to enable it to exercise corporate powers, and which cannot be supplied. "Whenever a corporation is reduced to

37 Brooklyn Steam Transit Co. v. that its charter shall terminate Smith's Cas. 365.

When the charter of a railroad company requires it to begin the 38 New York & Long Island construction of its road and expend thereon a certain per cent. 540, 1 Smith's Cas. 367. See post, in a certain time, and provides cited.

City of Brooklyn, 78 N. Y. 524, 1 if it fails to do so, it cannot retain its corporate existence after fail-As to the construction of such ure to comply with the requireprovisions, see, in addition to the ment by granting to another cases cited in this, and the note company the privilege of laying preceding, Bywaters v. Paris & tracks over such parts of its route Great Northern Ry. Co., 73 Tex. as the other company may desire to use. In re Brooklyn, Winfield & Newtown R. Co., 81 N. Y. 69.

of the amount of its capital with- § 313(b), and many cases there

such a state as to be incapable of acting or continuing itself it is dissolved."39

Thus, a corporation, other than a joint-stock corporation, is dissolved by the death or withdrawal of all its members, or of such a number of its members that too few remain, under the constitution of the corporation, to continue the succession, and fill vacancies. 40 "If a corporation," it was said in a New York case, "consists of several integral parts, and some of those are gone, and the remaining parts have no power to supply the deficiency, the corporation is dissolved. As in the case in where the corporation was to be composed Rolle,41 of a certain number of brothers, and a certain number of sisters. and all the sisters were dead, and it was admitted that all grants and acts done by the brothers afterwards were void; for, after the sisters were dead, it was not a perfect corporation. But the case which is immediately afterwards stated by Rolle, shows that if the brothers had possessed the power to appoint other sisters in the place of those who were dead, the corporation might have been revived. So, Baron Comyn says, if a corporation refuses to continue the election of officers till all die who could make an election, the corporation is dissolved."42

A corporation, however, is not dissolved by the destruction or loss of an integral part, if the remaining parts have the power to restore or renew the defective or deficient part.43 Thus, as is shown in the case referred to in the above quotation, the death or withdrawal of members does not dissolve a corporation, so long as a sufficient number remain to continue the succession and fill up vacancies.44 And a corporation is

<sup>39</sup> Buller, J., in Rex v. Pasmore, of McIntire Poor School v. Zanes-3 Term R. 245. And see Penobville Canal & Mfg. Co., 9 Ohio, scot Boom Corp. v. Lamson, 16 203, 34 Am. Dec. 436.

Me. 224, 33 Am. Dec. 656; Chesapeake & Ohio Canal Co. v. Balti-42 Philips v. Wickham, 1 Paige more & Ohio R. Co., 4 Gill & J. (Md.) 1.

<sup>40</sup> Blackwell v. State, 36 Ark. 178; Philips v. Wickham, 1 Paige (N. Y.) 590; Chesapeake & Ohio 44 Blackwell v. State, 36 Ark. Canal Co. v. Baltimore & Ohio R. 178; McGinty v. Athol Reservoir

<sup>(</sup>N. Y.) 590, 596.

<sup>43</sup> Smith v. Smith, 3 Desaus, Eq. (S. C.) 557, and cases cited in the notes following.

Co., 4 Gill & J. (Md.) 1; Trustees Co., 155 Mass. 183 (where the

not dissolved by the death, ineligibility, or withdrawal of its officers, or by a failure to elect officers, for however long a time, so long as there are members of the corporation with power to elect officers.<sup>45</sup>

Modern joint-stock corporations cannot be dissolved by the death of members, for, on the death of a stockholder, his shares, being property, will pass to his personal representative or legatee, who will thereupon take his place as a stockholder and

owners of certain mills died after being incorporated, but without having issued any stock); State v. Trustees of Vincennes University, 5 Ind. 77; Tomlinson v. Bricklayers' Union No. 1, 87 Ind. 308, 1 Cum. Cas. 33; State v. Societe Republicaine, 9 Mo. App. 114; Humphreys v. Stevens, 49 Ind. 491. 45 United States: Swan Land &

Cattle Co. v. Frank, 39 Fed. 456. Connecticut: Evarts v. Killingworth Mfg. Co., 20 Conn. 447.

Delaware: Higgins v. Downward, 8 Houst. 227, 40 Am. St. Rep. 141.

District of Columbia: United States Electric Lighting Co. v. Leiter, 19 D. C. 575.

Illinois: Baker v. Backus' Adm'r, 32 Ill. 79.

Iowa: Muscatine Turn Verein v. Funck, 18 Iowa, 469.

Kansas: Eureka Light & Ice Co. v. City of Eureka, 5 Kan. App. 669.

Kentucky: Wier v. Bush, 4 Litt.

Louisiana: In re Belton, 47 La. Ann. 1614; Cucullu v. Union Ins. Co., 2 Rob. 571; Brown v. Union Ins Co., 3 La. Ann. 177.

Massachusetts: Boston Glass Manufactory v. Langdon, 24 Pick. 49, 35 Am. Dec. 292, 2 Smith's Cas. 604, 1 Cum. Cas. 478; Russell v. McLellan, 14 Pick. 63; Knowlton v. Ackley, 8 Cush. 93; Packard v. Old Colony R. Co., 168 Mass. 92. Michigan: Cahill v. Kalamazoo

Michigan: Cahill v. Kalamazoo Mutual Ins. Co., 2 Doug. 124, 140, 43 Am. Dec. 457.

Mississippi: Smith v. Natchez 669.

Steamboat Co., 1 How. 479; Harris v. Mississippi Valley & Ship Island R. Co., 51 Miss. 603.

Missouri: St. Louis Domicile & Savings Loan Ass'n v. Augustin, 2 Mo. App. 123; Kansas City Hotel Co. v. Sauer, 65 Mo. 288.

New Jersey: Hoboken Building Ass'n v. Martin, 13 N. J. Eq. 427. New York: Trustees of Vernon Society v. Hills, 6 Cow. 23, 16 Am. Dec. 429; Philips v. Wickham, 1 Paige, 590; Allen v. New Jersey Southern R. Co., 49 How. Pr. 14; Kelsey v. Pfaudler Process Fermentation Co., 45 Hun, 10.

Pennsylvania: Rose v. Roseburg & Mercer Turnpike Co., 3 Watts, 46; Lehigh Bridge Co. v. Lehigh Coal & Nav. Co., 4 Rawle, 9, 26 Am. Dec. 111; Com. v. Cullen, 13 Pa. St. 133, 53 Am. Dec. 450.

South Carolina: Smith v. Smith, 3 Desaus. Eq. (S. C.) 557.

Tennessee: Blake v. Hinkle, 10 Yerg. 218; Lynch v. Lafland, 4 Cold. 96; Nashville Bank v. Petway, 3 Humph. 524; Parker v. Bethel Hotel Co., 96 Tenn. 252.

See, however, Lea v. Hernandez, 10 Tex. 137.

The removal of the officers of a corporation from the state, or their nonresidence, does not affect its corporate existence, though a statute or the charter may require officers to be residents of the state. Directors of Maryville College v. Bartlett, 8 Baxt. (Tenn.) 231; Eureka Light & Ice Co. v. City of Eureka, 5 Kan. App. 669.

member. 46 Nor is a joint-stock corporation dissolved by the fact that all the shares of its capital stock have come into the hands of a single stockholder, or of a less number of stockholders than were required by the statute in the formation of the corporation,47 although, under such circumstances, corporate action may be suspended.48

Injunction against use of name.—An injunction restraining a corporation from using its name, because of its similarity to that of another corporation, does not operate as a dissolution, where it is within the power of the corporation to choose another name.49

# § 308. Dissolution of corporation by surrender of charter.

In England, a corporation created by the king could be dissolved by the surrender of its charter and acceptance of the surrender by the king; and a corporation created by parliament could be dissolved by such a surrender and its acceptance by parliament. In this country, a corporation may certainly be dissolved by the surrender of its charter to the state by which it was created, and acceptance of its surrender by the state, or by such a surrender under authority of a statute previously enacted, which is equivalent to an acceptance by the state.50

46 Boston Glass Manufactory v. Bank of Gadsden v. Winchester, Langdon, 24 Pick. (Mass.) 49, 35 119 Ala. 168, 72 Am. St. Rep. 904; Am. Dec. 292, 2 Smith's Cas. 604, Cum. Cas. 478. See chapter

xxiii. <sup>47</sup> In re Belton, 47 La. Ann. 1614; Swift v. Smith, 65 Md. 428, 57 Am. Rep. 336; Russell v. Mc-Lellan, 14 Pick. (Mass.) 63, 69; Harrington v. Connor, 51 Neb. 214; Parker v. Bethel Hotel Co., 96 Tenn. 252; Wilde v. Jenkins, 4 Paige (N.Y.) 481; Newton Mfg. Co. v. White, 42 Ga. 148, 159; Louis-

Louisville Gas Co. v. Kaufman (Ky.) 48 S. W. 434.

The dictum to the contrary in re Bellona Co., 3 Bland (Md.) 442. cannot be sustained.

48 Swift v. Smith, 65 Md, 428, 57

Am. Rep. 336. 49 Armington v. Palmer, 21 R. I

See ante, § 53.

50 Taylor v. Holmes, 14 Fed. 498; Greeley v. Smith, 3 Story, 657, Fed. ville Banking Co. v. Eisenman, 94 Cas. No. 5,748; Enfield Toll Bridge Ky. 83, 42 Am. St. Rep. 335; But- Co. v. Connecticut River Co., 7 ton v. Hoffman, 61 Wis. 20, 50 Am. Conn. 29; Mobile & Ohio R. Co. Rep. 131; Baldwin v. Canfield, 26 v. State, 29 Ala. 573; McMahon v. Minn. 43; Main v. Mills, 6 Biss. Morrison, 16 Ind. 172, 79 Am. Dec. 98, Fed. Cas. No. 8,974; First Nat. 418; Mariners' Bank v. Sewall, 50

The dissolution of a corporation by a surrender of its charter authorized or accepted by the state, though it may prevent existing creditors from suing the corporation, and may abate suits pending against it, and prevent the subsequent entry of a judgment against it, does not for this reason impair the obligation of contracts. "A corporation," said Mr. Justice Story in a leading case in the supreme court of the United States, "by the very terms and nature of its political existence, is subject to dissolution, by a surrender of its corporate franchises. and by a forfeiture of them for willful misuser and nonuser. Every creditor must be presumed to understand the nature and incidents of such a body politic, and to contract with reference to them. And it would be a doctrine new in the law, that the existence of a private contract of the corporation should force upon it a perpetuity of existence contrary to public policy, and the nature and objects of its charter."51 Furthermore, the creditors of a dissolved corporation, if no remedy is given them by statute, have a remedy in equity to reach its assets and subject them to the satisfaction of their claims. 52

Transfers of property and franchises under legislative authority.—If a statute authorizes a corporation to transfer, not only its property, but also its franchises, including its franchise to be a corporation, a transfer in pursuance of the statute is, in effect, a surrender of its charter with the consent of the legislature, and operates as a dissolution.<sup>53</sup> And the same is true

Me. 220; Revere v. Boston Cop- by the legislature. per Co., 15 Pick. (Mass.) 351; Jefferson College, 63 Pa. St. 428. Trisconi v. Winship, 43 La. Ann. A resolution by the stockholde: 45, 26 Am. St. Rep. 175; Lauman of a corporation to discontinue i v. Lebanon Valley R. Co., 30 Pa. business, under a statute authori St. 42, 72 Am. Dec. 685; Houston v. Jefferson College, 63 Pa. St. 428; Wilson v. Proprietors of Central Bridge, 9 R. I. 590; Attorney General v. Clergy Society, 10 Rich. Eq. (S. C.) 604; Combes v. Keyes, 89 Wis. 297, 46 Am. St. Rep. 839.

The legislature may permit a corporation to surrender its charter, where there is a provision in the charter that it shall not be alled in any other manner than R. Co. v. Kyle, 9 Lea (Tenn.) 691.

A resolution by the stockholders of a corporation to discontinue its business, under a statute authorizing such a resolution, has been held to be a voluntary surrender of the corporate franchise, and a dissolution of the corporation. Law v. Rich (W. Va.) 35 S. E. 858.

 Mumma v. Potomac Co., 8 Pet.
 (U. S.) 281, 2 Smith's Cas. 614, 1 Cum. Cas. 459.

52 Post, § 326.

of a sale of all the property and franchises of a corporation, under legislative authority, or execution, or under a decree of foreclosure of a mortgage given by the corporation, or a decree to enforce a statutory lien of the state,54 unless the franchise to be a corporation is expressly excluded from the sale.<sup>55</sup> transfer of the entire property of a corporation, under legislative authority, to another corporation, operates as a dissolution of the former, where it is unable to continue the exercise of its corporate powers without the possession of such property.<sup>56</sup>

Consolidation of corporations.—As we shall see in another chapter, the legislature may authorize existing corporations to consolidate, and the consolidation will dissolve one or both of the consolidating corporations. If both surrender their charters and organize under a new charter, both are dissolved, and a new corporation is created, while, if one merely transfers

Reifler v. Honesdale & Delaware Plank Road Co., 1 Pa. Co. Ct. R. 64; Reynolds v. Cridge, 11 Pa. Co. Ct. R. 306.

Compare Cape Fear & Deep River Nav. Co. v. Costen, 63 N. C.

54 Rogersville & Jefferson R. Co. v. Kyle, 9 Lea (Tenn.) 691; Reifler v. Honesdale & Delaware Plank Road Co., 1 Pa. Co. Ct. R. 64; Reynolds v. Cridge, 11 Pa. Co. Ct. R. 306; White Mountains Railroad v. White Mountains (N. H.) Railroad, 50 N. H. 50.

As to the effect of a conveyance of a railroad, under the North Carolina statute, in pursuance of a sale under a mortgage, see James v. Western North Carolina R. Co.,

121 N. C. 523, 530.

A statute providing that a corporation shall be dissolved by a mortgage sale of its franchises and property does not terminate the existence of the company until after a legal and valid sale. An illegal and fraudulent sale does not work a dissolution. Mountains Railroad v. White White Mountains (N. H.) Railroad, 50 N. H. 50.

A corporation is not dissolved by the fact that all its property and franchises are held in custody by a court of equity for the purpose of enforcing satisfaction of claims against them. Heath v. Missouri, Kansas & T. Ry. Co., 83 Mo. 617.

<sup>55</sup> In Higgins v. Downward, 8 Houst. (Del.) 227, 40 Am. St. Rep. 141, where, under a decree of a federal court, a railroad company's road and all its rights, privileges, immunities, and franchises, "exclusive of those granted by the state," were sold to satisfy a mortgage, and the legislature afterwards incorporated the purchasers, and vested them with all the rights, title, interest, property, possession, claims, demands at law or in equity of, in, or to such road, with its appurtenances, and with all the rights, powers, immunities, privileges, and chises of the corporation as whose property it was sold, it was held that the act did not revoke the charter of the railroad company, or operate as a dissolution.

56 Stone v. Inhabitants of Framingham, 109 Mass. 303.

its property to the other in return for stock in the latter issued to the stockholders of the former, the former only is dissolved.<sup>57</sup>

Necessity for acceptance or consent of the state.—There is dictum in many of the cases to the effect that the stockholders of a purely private corporation, owing no special duties to the public, may voluntarily surrender their charter and dissolve, without the consent of, or acceptance of the surrender by, the state, provided they act in good faith and without prejudice to creditors; and there are some actual decisions to this effect.<sup>58</sup> In an Alabama case, for example, it was held squarely that a private corporation, organized under a general law for the purpose of conducting a purely private enterprise, entered upon solely for the benefit of the shareholders, and which is under no duty to the public which would not equally obtain if the stockholders had formed an unincorporated association or partnership for the same objects, may be dissolved at any time by the stockholders without obtaining the consent of the state; and that the duration of its corporate existence may be limited by a by-law adopted at the time of organization. It was further held that such a by-law, providing that the corporation shall be dissolved on a certain day, puts an end to the corporation on that day, and that, if the stockholders afterwards continue business as before, they do so as a mere unincorporated association.59

57 Shields v. Ohio, 95 U. S. 319; Lauman v. Lebanon Valley R. Co.,

subject, post, § 347 et seq.; and sociation sold out and assigned as to the effect of consolidation as in writing all its claims for un-

v. Waganer, 71 Ala. 581.

30 Pa. St. 42, 72 Am. Dec. 685. In a Georgia case it was held See for a full treatment of this that where a building and loan asas to the effect of consolidation as a dissolution, see post, § 354.

58 People v. Trustees of College of California, 38 Cal. 166; Fish v. Nebraska City Barb-Wire Fence Co., 25 Fed. 795; Lauman v. Lebanon Valley R. Co., 30 Pa. St. 42, 72 Am. Dec. 685; Merchants' & Planters' Line v. Wagner, 71 Ala. 581; Moore v. Whitcomb, 48 Mo. 543. And see Pringle v. Eltringham Construction Co., 49 La. Ann. 301; Van Pelt v. Home Building & Loan Ass'n, 87 Ga. 370.

This view cannot be sustained on principle, and the decisions in which it has been recognized are not supported by authority. When a corporation is created, whether by a special charter or under a general law, and whether its object be purely private, as in the case of a manufacturing company, or quasi public, as in the case of a railroad company, there is, in a sense, a contract between the corporation and the state, and this contract cannot be terminated, any more than any other contract, by one of the parties without the consent of the other, given either at the time the corporation is formed or afterwards. According to the weight of authority, therefore, a corporation, while it may dispose of its property and cease to do business under some circumstances, cannot be legally dissolved by a resolution of the stockholders or members, and a surrender of its charter, unless the surrender is authorized by some statute, or is afterwards accepted or ratified by the state.60

"Charters," said Judge Morton in a leading Massachusetts case, "are in many respects compacts between the government and the corporators. And as the former cannot deprive the latter of their franchises in violation of the compact, so the latter cannot put an end to the compact without the consent of the former. It is equally obligatory on both parties. surrender of a charter can only be made by some formal sol-

Ga. 370.

60 Boston Glass Manufactory v. Langdon, 24 Pick. (Mass.) 49, 35 Am. Dec. 292, 2 Smith's Cas. 604, 1 Cum. Cas. 478. See, also, Mumma v. Potomac Co., 8 Pet. (U. S.) 281, 2 Smith's Cas. 614, 1 Cum. Cas. 459; Taylor v. Holmes, 14 Fed. 498; Evarts v. Killingworth Ann. 27; Riddle v. Proprietors of Revere v. Boston Copper Co., 15 in note 87, infra.

Home Building & Loan Ass'n, 87 Pick. (Mass.) 351; Town v. Bank of River Raisin, 2 Doug. (Mich.) 530; Campbell v. Mississippi Union Bank, 6 How. (Miss.) 681; Rorke v. Thomas, 56 N. Y. 559; McLaren v. Pennington, 1 Paige (N. Y.) 107; Wilson v. Proprietors of Central Bridge, 9 R. I. 590; La Grange & Memphis R. Co. v. Rainey, 7 Cold. (Tenn.) 420; Norris v. Town of Smithville, 1 Swan (Tenn.) 164; Mfg. Co., 20 Conn. 448; Enfield Attorney General v. Superior & Toll Bridge Co. v. Connecticut St. Croix R. Co., 93 Wis. 604; Peo-River Co., 7 Conn. 29, 45; Meple v. Ballard, 134 N. Y. 269; Tochanics' Bank v. Heard, 37 Ga. peka Paper Co. v. Oklahoma Pub-401; Curien v. Santini, 16 La. lishing Co., 7 Okla. 220.

Compare Slee v. Bloom, 5 Johns. Locks and Canals on Merrimack Ch. (N. Y.) 366, 19 Johns. (N. Y.) River, 7 Mass. 169, 5 Am. Dec. 35; 456, 2 Cum. Cas. 113, referred to

emn act of the corporation; and will be of no avail until accepted by the government. There must be the same agreement of the parties to dissolve, that there was to form the compact. It is the acceptance which gives efficacy to the surrender. dissolution of a corporation, it is said, extinguishes all its debts. The power of dissolving itself by its own act, would be a dangerous power, and one which cannot be supposed to exist."61 This language was with reference to a purely private manufacturing corporation.

Dissolution distinguished from sale of property and cessation of business.—The error in assuming or holding in some of the cases that a corporation may be voluntarily dissolved without authority from the state has resulted to a great extent, no doubt, from failure to distinguish the dissolution of a corporation from the mere disposal of its property and cessation of business. the law, they are very different, and to say that a corporation may dispose of all its property and cease to do business does not at all imply that it may dissolve, and thereby cease to exist. As we have seen in another chapter, a purely private corporation, owing no special duties to the public, may dispose of all its property, divide the proceeds among its stockholders, and cease to do the business for which it was organized, if its creditors are not prejudiced thereby.62

This, however, does not dissolve the corporation in contemplation of the law, for it is well settled that it may exist without property and without doing business.63 It could still sue and be sued, if the occasion for suit should arise,64 and the state could institute proceedings to forfeit its charter. 65 And, in the absence of such proceedings, there is no principle of law which would prevent it from again acquiring property and resuming

<sup>&</sup>lt;sup>61</sup> Boston Glass Manufactory v. Langdon, 24 Pick. (Mass.) 49, 35 Langdon, 24 Pick. (Mass.) 49, 35 Am. Dec. 292, 2 Smith's Cas. 604, Languon, 24 Figh. (Mass.) 70, 60

Am. Dec. 292, 2 Smith's Cas. 604, 1 Cum. Cas. 478; Muscatine West1 Cum. Cas. 478.

62 Ante. § 160.

33; post, §§ 309, 310, and cases 1 Cum. Cas. 478.

62 Ante, § 160.

63 Post, §§ 309, 310.

64 Boston Glass Manufactory v.

there cited. 65 Post, § 314(f), (i).

business.66 Obviously, this is altogether inconsistent with a "dissolution," in the legal sense. As has been said by Mr. Morawetz, "a corporation may be dissolved de facto before its legal right to exist has expired, and before it is dissolved de iure."67

In accordance with this view, it has been held that all the stockholders in a corporation may, by mutual agreement, cancel their shares, wind up the business of the corporation, and distribute its property, and thus cease longer to exist as a corporation in fact; but if the surrender of their charter is not accepted or authorized by the state, the corporation still exists in contemplation of the law, and may sue and be sued in the courts.<sup>68</sup> In the absence of statutory provision therefor, a corporation is not dissolved by the vote of its members to dissolve it and close its concerns, followed by a transfer of all its property to trustees, and by notice to the executive department of the government that it claims no further interest in its charter. 69 Voluntary dissolution of a corporation and surrender of its charter, without the consent of the state, does not destroy the corporation so as to take away its power to act for the purpose of winding up its affairs, or so as to deprive creditors of their remedies against it.70

Presumption from nonuser of franchises.—As we shall see in other sections, failure of a corporation to elect officers or to exercise the powers conferred upon it by its charter may be

Waganer, 71 Ala. 581, was wrongly decided.

67 2 Morawetz, Corp. § 962.

68 Boston Glass Manufactory v. Langdon, 24 Pick. (Mass.) 49, 35 Am. Dec. 292, 2 Smith's Cas. 604, 1 Cum. Cas. 478; Evarts v. Killingworth Mfg. Co., 20 Conn. 448; Rorke v. Thomas, 56 N. Y. 559; Allen v. New Jersey Southern R. constructing its road. Muscatine Co., 49 How. Pr. (N. Y.) 14; Hol-Western R. Co. v. Horton, 38 Iowa, lingshead v. Woodward, 35 Hun 33.

66 For this reason, the case of (N. Y.) 410; and cases cited post, Merchants' & Planters' Line v. §§ 309, 310. §§ 309, 310.

69 Revere v. Boston Copper Co., 15 Pick. (Mass.) 351.

70 Muscatine Turn Verein v. Funck, 18 Iowa, 469.

Even if a sale by a railroad corporation of its property be regarded as a voluntary dissolution, the corporation continues in existence to such an extent at least as to enable it to enforce its rights to a tax voted by a county to aid in ground for proceedings by the state to forfeit its charter for. nonuser,71 but it does not of itself, and in the absence of such proceedings and a judgment of forfeiture, result in a dissolution of the corporation, where there is in fact no surrender of its charter and acceptance of the surrender by the state. 72 Nonuser of its franchises by a corporation, however, if it is continued for a long time, will raise a presumption that there has been such a surrender, and that it has been authorized or accepted by the state.73

Who may surrender charter.—A surrender of the charter of a corporation it not within the authority of the directors or managing officers. It must be by the stockholders.74

Whether or not a majority of the stockholders of a corporation have the power to surrender its charter and dissolve under authority from the legislature depends upon the circumstances. A majority of the stockholders of a corporation may abandon the enterprise, sell out the property of the corporation, and surrender the charter or dissolve under legislative authority, if no time is specified in the charter for continuance of the enterprise, provided the enterprise can no longer be continued profitably.75 When a time for the continuance of a corporation is

<sup>71</sup> Post, § 314(c), (f). 72 Post, § 309.

<sup>73</sup> State v. Trustees of Vincennes University, 5 Ind. 77; Brandon Iron Co. v. Gleason, 24 Vt. 228; Strickland v. Prichard, 37 Vt. 324; Hartford Bridge Co. v. Town of East Hartford, 16 Conn. 149; Combes v. Keyes, 89 Wis. 297, 46 Am. St. Rep. 839.

Where a railroad company had been divested by judicial sale of all its property, and for twenty-six years had neither owned propsix years had neither owned property nor done business in the state, cennes University, 5 Ind. 77. nor elected officers or kept any 74 Jones v. Bank of Leadville, 10 officer therein, it was held that a surrender of its charter and ac-ceptance by the state would be presumed. Combes v. Keyes, 89 Wis. 297, 46 Am. St. Rep. 839.

franchise is one of intention, and therefore an abandonment is not conclusively shown by nonuser, even for a long time. Raritan Water Power Co. v. Veghte, 21 N. J. Eq. 463; Taylor v. Holmes, 14 Fed. 498.

The presumption of the dissolution of a corporation arising from nonuser of its franchises for a long period of time is rebutted by recent acts of the legislature recognizing its existence as con-

Colo. 464. And see Bank Commissioners v. Bank of Brest, Har. Ch. (Mich.) 106; Smith v. Smith, 3 Dessaus. (S. C.) 557.

Wis. 297, 46 Am. St. Rep. 839.

The question, however, whether a corporation has abandoned its

See chapter xxiv.

75 Black v. Delaware & Raritan
Canal Co., 22 N. J. Eq. 130.

fixed by its charter, the charter cannot be surrendered and the corporation dissolved except by the unanimous consent of all the stockholders. A majority cannot dissolve against the dissent of the minority.76

In some states there is a statutory provision that no corporation can be dissolved prior to the period fixed in the articles of association or incorporation except by unanimous consent of the stockholders, unless a different rule has been adopted in the articles.77

Voluntary dissolution under statutory authority.-In most of the states the legislatures have enacted statutes allowing the voluntary dissolution of private corporations, and prescribing the mode in which such a dissolution may be effected. statute, of course, is equivalent to acceptance by the legislature of the surrender of a charter; but the winding up and dissolution, to be effectual, must be in compliance with the terms of the statute.<sup>78</sup> These statutes vary in the different states. In some states the dissolution may be effected by the action of the stockholders alone. In others it may be effected by an application to and order of some court, or by a bill in equity, or suit under the code, etc., in which the court makes an order or decree of dissolution, if satisfied that it is to the interest of

post, chapter xxiv.

dissolution only. It does not prohibit a sale of the property of a corporation, or a suspension of its business, for this does not dissolve the corporation. Price v. Holcomb, 89 Iowa, 123.

See post, §§ 309, 310.

78 See Riddell v. Harmony Fire Co., 28 Leg. Int. (Pa.) 356; Com. v. Slifer, 53 Pa. St. 71.

stockholders of a corporation to effect a dissolution of the corporation, pay its debts, sell its property, and distribute the proceeds ket Co., 190 Pa. St. 124.

78 Barton v. Enterprise Loan & among the stockholders, has no au-Building Ass'n, 114 Ind. 226, 5 Am. thority to distribute such proceeds St. Rep. 608. On this point, see until dissolution, as provided by law, with an exhibition of ac-77 Such a provision applies to counts, and an opportunity for creditors to present their claims. In re Lincoln Market Co., 190 Pa. St. 124.

A committee appointed by stockholders of a company to effect a dissolution of the company, exchange its property for stock in another company, which has a mere speculative value, and to distribute the stock, or the proceeds there-A committee appointed by the of, is not liable to the stockholders for mere error of judgment in holding the stock until it depreciates in value. In re Lincoln Marthe stockholders, and that it will not prejudice the interests of the public. 79

When a statute authorizes the surrender of its franchises by a corporation, and proceedings to be had for the winding up

79 As to such statutes in particular states, see Trisconi v. Winship, 43 La. Ann. 45, 26 Am. St. Rep. 175; In re Niagara Ins. Co., 1 Paige (N. Y.) 258; Com. v. Slifer, 53 Pa. St. 71.

In New York, the Code of Civil Procedure (sections 2419-2431) provides for the voluntary dissolution of a corporation upon a petition to the supreme court by a majority of the directors, trustees, or other managing officers, if they "discover that the stock, effects, and other property thereof are not sufficient to pay all just demands, for which it is liable, or to afford a reasonable security to those who may deal with it; or if, for any reason, they deem it beneficial to the interests of the stockholders, that the corporation should be dissolved." Provision is also made for cases in which the directors or trustees are equally divided.

As to the proceedings under this statute, see Hitch v. Hawley, 132 N. Y. 212; In re Peekamose Fishing Club, 151 N. Y. 511; Moore v. Potter, 155 N. Y. 481; In re Board of Directors of Broadway Ins. Co.,

23 App. Div. (N. Y.) 282. In Hitch v. Hawley, 132 N. Y. 212, it was held that, where it appears that the interests of the stockholders of a corporation are so discordant as to prevent efficient management, and that a large majority of its trustees and members wish to wind up its affairs by a dissolution, the fact is established that a dissolution will be for the interests of the stockholders, within the meaning of the above stat-And it was held, therefore, that a corporation organized under the law providing for the organization of exchanges or boards of trade might be dissolved by the court on petition of a majority of to resolve to dissolve the corporaits trustees and members, where it tion, and divide the property re-

appeared that it was doing no business because of the diverse interests of its members, although it was solvent, and a minority of the trustees and members opposed the dissolution.

As to the requisites of a petition for voluntary dissolution under the New York statute, and inventory of property, debts, etc., see In re Westchester Iron Co., 6 Abb. Pr. (N. Y.) 386, note; In re Dubois, 15 How. Pr. (N. Y.) 7; In re Santa Eulalia Silver Mining Co., 51 Hun (N. Y.) 640; In re Hitchcock Mfg. Co., 1 App. Div. (N. Y.) 164.

On a petition for the voluntary dissolution of a corporation in New York, under section 2419 et seq. of the Code of Civil Procedure, the court acquires no jurisdiction unless the petition is verified by a majority of the directors of the corporation, as required by that statute. In re Dolgeville Electric Light & Power Co., 160 N. Y. 500, reversing 41 App. Div. 624, 58 N.

Y. Supp. 1139.

The commencement of proceedings under the New York statute for the voluntary dissolution of a corporation, the appointment of a receiver, and the making of the usual order restraining all persons from disposing of any of the property of the corporation, except to deliver it to the receiver, does not prevent one with whom the corporation has made a contract for the purchase of personal property, and which it has refused to take and pay for, from such property, upon notice to the receiver, and holding him for the balance. Moore v. Potter, 155 N. Y. 481, reversing 87 Hun, 334.

Under a statute allowing the stockholders of a corporation, by a majority vote in general meeting. of its affairs, such surrender and proceedings are effectual to dissolve the corporation, without any acceptance of the surrender by the state.80

Injunction against dissolution.—It has been held that where a corporation is defendant in a suit in equity, and may be held liable to respond pecuniarily, it may be enjoined from taking steps to procure its own dissolution, and thus defeat the object of the suit.81

#### § 309. Suspension of business and nonuser of franchises.

(a) In general.—Since, as we have seen in the preceding section, the stockholders of a corporation cannot dissolve it by a surrender of the charter and franchises, unless the surrender is accepted by the state or authorized by some statute,82 it necessarily follows that a corporation is not dissolved by the mere failure to exercise the powers conferred upon it by its charter, or by its abandonment of the corporate enterprise after having commenced the exercise of the powers conferred upon it. Such nonuser is ground for a proceeding by the state to forfeit its charter,83 and, if it has continued for a long time, may raise a presumption of a surrender of the charter and acceptance of

third in interest of the stockholders to file their bill for dissolution, the stockholders may file a bill for dissolution notwithstanding the directors have made an assignment of all the property of the corporation, and abandoned its business, and such action has been ratified at a general meeting of the stockholders, as this does not dissolve the corporation. Weigand v. Alliance Supply Co., 44 W. Va.

80 Wilson v. Proprietors of Central Bridge, 9 R. I. 590.

Where it appeared that the stockholders of a corporation voted to divide its assets, and its dividend book showed such division in pursuance of a vote of the directors,

maining after payment of debts, signed by all the stockholders exand allowing not less than one cept one, and the stockholders' receipts for the dividend provided that, in case any claims should run against the company which its remaining assets should be insufficient to meet, each stockholder would pay his portion of the defi-ciency, it was held that this showed that the corporation was winding up its affairs, as permitted by the Maine statutes, and not merely making a dividend from annual earnings. Buck v. Merchants' Mutual Marine Ins. Co., 68 Me. 532.

> 81 Fisk v. Union Pacific R. Co.,10 Blatchf. 518, Fed. Cas. No. 4.830.

82 Ante, § 308.

83 Post, § 314(c).

the surrender by the state; <sup>84</sup> but it does not *ipso facto* cause a dissolution. <sup>85</sup> A corporation is not even dissolved by an injunction restraining it from the exercise of its corporate franchises, and depriving it of its property. <sup>86</sup>

Cessation or abandonment of its business by a corporation may amount to a dissolution in such a sense and to such an extent as to render applicable a statute imposing individual liability upon stockholders for the debts of the corporation, and allowing creditors to sue them.<sup>87</sup> This is true by express pro-

84 Ante, § 308, note 73. 84 Ante, § 308, note 73.
85 Boston Glass Manufactory v.
Langdon, 24 Pick. (Mass.) 49, 35
Am. Dec. 292, 2 Smith's Cas. 604,
1 Cum. Cas. 478. See, also, Swan
Land & Cattle Co. v. Frank, 39
Fed. 456; Bradley v. McKee, 5
Cranch, C. C. 298, Fed. Cas.
No. 1,784; Kanawha Coal Co.
v. Kanawha & Ohio Coal Co.,
7 Blatchf. 391, Fed. Cas. No. 7,606;
Davis v. Memphis & Charleston R Davis v. Memphis & Charleston R. Co., 87 Ala. 633; State v. Real Estate Bank, 5 Ark. 595, 41 Am. Dec. 109; Evarts v. Killingworth Mfg. Co., 20 Conn. 448; United States Electric Lighting Co. v. Leiter, 19 D. C. 575; Reichwald v. Commercial Hotel Co., 106 III. 439; John v. Farmers' & Mechanics' Bank, 2 Blackf. (Ind.) 367, 20 Am. Dec. 119; Valley Bank & Savings Institution v. Ladies' Consavings institution v. Ladies' Congregational Sewing Society, 28 Kan. 423; Rollins v. Clay, 33 Me. 132; Proprietors of Baptist Meeting-House v. Webb, 66 Me. 398; Regents of University of Maryland v. Williams, 9 Gill & J. (Md.) 365, 31 Am. Dec. 72; Russell v. McLellan, 14 Pick. (Mass.) 63; Knowledge, V. Ackley, 8 Cueb. (Mass.) 92. ton v. Ackley, 8 Cush. (Mass.) 93; State Nat. Bank of St. Joseph v. Robidoux, 57 Mo. 446; Kansas City Hotel Co. v. Sauer, 65 Mo. 279; Bradt v. Benedict, 17 N. Y. 93; Kincaid v. Dwinelle, 59 N. Y. 548; Allen v. New Jersey Southern R. Co., 49 How. Pr. (N. Y.) 14; Lake Ontario Nat. Bank v. Onondaga County Bank, 7 Hun (N. Y.) 549; State v. Rives, 5 Ired. (N. C.) 297;

107 N. C. 581; Jones v. Spartanburg Herald Co., 44 S. C. 526; Parker v. Bethel Hotel Co., 96 Tenn. 252; Bache v. Nashville Horticultural Soc., 10 Lea (Tenn.) 436; Directors of Maryville College v. Bartlett, 8 Baxt. (Tenn.) 231; Moseby v. Burrow, 52 Tex. 396; Brandon Iron Co. v. Gleason, 24 Vt. 228; Weigand v. Alliance Supply Co., 44 W. Va. 133; Attorney General v. Superior & St. Crix R. Co., 93 Wis. 604; Sleeper v. Goodwin, 67 Wis. 577.

See, also, Attica State Bank v. Benson, 8 Kan. App. 566; Brigham v. Nathan (Kan.) 62 Pac. 319; Jones v. Edson (Kan. App.) 62 Pac. 249; Salina Nat. Bank v. Prescott, 60 Kan. 490; Richards v. Minnesota Savings Bank, 75 Minn. 196; Witherow v. Slayback, 158 N. Y. 649; Topeka Paper Co. v. Oklahoma Publishing Co., 7 Okla. 220; Law v. Rich (W. Va.) 35 S. E. 858; Pritchard v. Barnes, 101 Wis. 86.

86 Kincaid v. Dwinelle, 59 N. Y. 548.

31 Am. Dec. 72; Russell v. Mc-Lellan, 14 Pick. (Mass.) 63; Knowlton v. Ackley, 8 Cush. (Mass.) 93; State Nat. Bank of St. Joseph v. Robidoux, 57 Mo. 446; Kansas City Hotel Co. v. Sauer, 65 Mo. 279; showing that it intended to conbradt v. Benedict, 17 N. Y. 93; thue business, might be consid-kincaid v. Dwinelle, 59 N. Y. 548; ered dissolved to such an extent Allen v. New Jersey Southern R. Co., 49 How. Pr. (N. Y.) 14; Lake Ontario Nat. Bank v. Onondaça for its debts under a statute making stockholders of a corporation County Bank, 7 Hun (N. Y.) 549; by the company "at the time of its Heggie v. Building & Loan Ass", dissolution," to the extent of their

vision of some of the statutes.88 Under such statutes, however, the suspension of business does not dissolve the corporation further than to allow enforcement of the stockholders' liability. It is not dissolved for all purposes.89

- (b) Failure to hold meetings.—The mere failure of a corporation to hold meetings, though the neglect has continued for a number of years, does not ipso facto work a dissolution of the corporation.90
- (c) Failure to elect officers.—Failure of a corporation to elect officers renders it inactive, and may be ground for proceedings to forfeit its charter, but such failure does not dissolve the corporation so long as it is within the power of the corporation to hold an election and supply the defect. "The condition of a corporation whose charter has expired is not the same as that of a corporation which has failed to elect its officers, and, as the consequence of that failure, is rendered inactive. The life of the one is out of it by its own constitution, and not from a failure to do what its charter enabled them to do, to give them active being; the other was entitled by its charter to a continued active life, but it has failed to continue that activity by the election of its necessary officers. Its active powers, but not its being, are gone. The one is dead; the other is dormant. The principles of law which apply to a corporation thus dormant or disabled are not the same as those which are applicable to the rights of a corporation which is dissolved, or civilly dead.

But in the later case of Bradt v. Benedict, 17 N. Y. 99, it was intimated that in Slee v. Bloom the court supplied what might be deemed a defect in the statute, rather than announced the law as it was found in the books, and it was held that the decision should not be carried beyond the precise facts upon which it rested. 88 Brigham v. Nathan (Kan.) 62

Pac. 319; Jones v. Edson (Kan.)
62 Pac. 249. See post, chapter xxv. forfeiture of the charter of a corsponent v. Edson (Kan.) 62 Pac. poration, see post, § 314.

respective shares of stock. See, 249; Sleeper v. Norris, 59 Kan. also, Briggs v. Penniman, 8 Cow. 555; Salina Nat. Bank v. Prescott, (N. Y.) 387, 18 Am. Dec. 454. 60 Kan. 490.

90 State v. Trustees of Vincen-30 State v. Trustees of Vincennes University, 5 Ind. 77; Smith v. Natchez Steamboat Co., 1 How. (Miss.) 479; Packard v. Old Colony R. Co., 168 Mass. 92; Parsons v. Eureka Powder Works, 48 N. H. 66; Eureka Light & Ice Co. v. City of Eureka, 5 Kan. App. 669. See, also, State v. Barron, 58 N. H. 370; State v. Societe Republicaine, 9 Mo. App. 114.

As to whether it is ground for

In the former case debts due are extinguiushed; 91 not so in the latter case."92

(d) Inability to continue business.—The fact that conditions have arisen which render a corporation unable to continue the business for which it was created may be ground for proceedings to dissolve the corporation,93 but it does not ipso facto result in a dissolution, where no integral part of the corporation has been destroyed or lost.94 Thus it has been held that a city's withdrawal of its aid and superintendence of an incorporated fire department, rendering the department inoperative, did not ipso facto work a forfeiture of the department's charter or a dissolution.95

### § 310. Alienation or loss of property and franchises.

In the absence of a surrender of its charter by a corporation and its acceptance by the state, or such a surrender under authority of a statute in force at the time, a corporation is not dissolved by the fact that it has not only ceased to exercise the powers conferred upon it by its charter, but has also disposed of all its property by absolute sale, or distributed it among its stockholders, or assigned it for the benefit of creditors, or leased it for a long term of years, or lost it, for a corporation may exist without property.96

92 Per Chancellor Saulsbury in Wilmington & Reading R. Co. v. Downward (Del.) 14 Atl. 720. See, also, Evarts v. Killingworth Mfg. Co., 20 Conn. 447; Trustees of Vernon Society v. Hills, 6 Cow. (N. Y.) 23, 16 Am. Dec. 429; and many other cases cited ante, § 307, note

The resignation of the officers of a corporation, said the Iowa ccurt, does not dissolve the corpo-The resignation of the officers of a corporation, said the Iowa ccurt, does not dissolve the corporation. "Officers and agents are necessary to the management of the affairs of such an organization, but the corporation may have, and does have, an existence per se, so as to maintain succession and hold of the Iowa columbus & X. R. Co., 1 Fed. 700; Bradley v. McKee, 5 Cranch, C. C. 298, Fed. Cas. No. 1,784; Swan Land & Cattle Co. v. Frank, 39 Fed. 456; Davis v. Memphis & Charleston R. Co., 87 Ala. 633; Evarts v. Killingworth Mfg. Co., as to maintain succession and hold

91 As to this, however, see post, and preserve its franchises, though its functions may, for the time being, be suspended for want of means of action." Muscatine Turn Verein v. Funck, 18 Iowa,

469, 472.
93 Post, § 314(g).
94 See Sleeper v. Goodwin, 67

95 Com. v. Reliance Fire Co., 31 Leg. Int. (Pa.) 46.

96 United States v. Little Miami,

It has been held, therefore, that a corporation does not cease to exist because it has stopped business, distributed its assets among its stockholders, and apportioned its debts among them, and that a note made by it afterwards is binding upon it.97 For the same reason, it has been held that a railroad company is not dissolved by the fact that it has made a lease for a long term of years of all its property; 98 that a corporation created for the purpose of owning and operating a mill is not dissolved by the burning of the mill and the loss of all its property; 99 and that a banking corporation is not dissolved by the fact that its assets are forced out of the state by military power. 100 In an action by a bridge company against a town on the latter's contract to purchase the former's bridge, it was held that the company's existence was not affected by the fact that it conveyed the bridge and its franchise to the town, when the bridge

Co. v. Town of Westport, 39 Conn. Hardware & Mfg. Co. v. James-337; Higgins v. Downward, 8 Spencer-Bateman Co., 15 Utah, Houst. (Del.) 227, 40 Am. St. Rep. 110; Weigand v. Alliance Supply 141; Reichwald v. Commercial Co., 44 W. Va. 133; Sleeper v. Hotel Co., 106 Ill. 439; Bruffett v. Goodwin, 67 Wis. 577. 337; Higgins v. Downward, 8 Houst. (Del.) 227, 40 Am. St. Rep. 141; Reichwald v. Commercial Hotel Co., 106 Ill. 439; Bruffett v. Great Western R. Co., 25 Ill. 353; De Camp v. Alward, 52 Ind. 468; Muscatine Western R. Co. v. Hor-ton, 38 Iowa, 33; Price v. Holcomb, ton, 38 Iowa, 33; Price v. Holcomb, 89 Iowa, 123; Eureka Light & Ice Co. v. City of Eureka, 5 Kan. App. 669; In re Belton, 47 La. Ann. 1614; State v. Bank of Maryland, 6 Gill & J. (Md.) 205, 26 Am. Dec. 561; Norris v. Trustees of Abingdon Academy, 7 Gill & J. (Md.) 7; Boston Glass Manufactory v. Langdon, 24 Pick. (Mass.) 49, 35 Am. Dec. 292, 2 Smith's Cas. 49, 35 Am. Dec. 292, 2 Smith's Cas. 604, 1 Cum. Cas. 478; Hill v. Fogg, 41 Mo. 563; Kansas City Hotel Co. v. Sauer, 65 Mo. 279; New Jersey Zinc Co. v. New Jersey Frank-linite Co., 13 N. J. Eq. 322; Sewell N. East Cape May Beach Co., 50 N. J. Eq. 717; Wilde v. Jenkins, 4 Paige (N. Y.) 481; Kincaid v. Dwinelle, 59 N. Y. 548; Troy & Rut-land R. Co. v. Kerr, 17 Barb. (N. Y.) 581; Brinckerhoff v. Brown, 7 Johns. Ch. (N. Y.) 217; State v. Rives, 5 1614. Ired. (N. C.) 297; Parker v. Bethel 100 Lane v. Bank o Hotel Co., 96 Tenn. 252; Weyeth 9 Heisk. (Tenn.) 419.

Goodwin, 67 Wis. 577.

See, also, Attica State Bank v. Benson, 8 Kan. App. 566; Witherow v. Slayback, 158 N. Y. 649; Topeka Paper Co. v. Oklahoma Publishing Co., 7 Okla. 220; Gulf, Colorado & S. F. Ry. Co. v. Newell, 73 Tex. 334, 15 Am. St. Rep. 788; Pritchard v. Barnes, 101 Wis. 86.

And See ante & 308; post & 214

And see ante, § 308; post, § 314. 97 Bradley v. McKee, 5 Cranch, C. C. 298, Fed. Cas. No. 1,784; and other cases in the note preceding. And see ante, § 308; post, § 314.

98 United States v. Little Miami. Columbus & X. R. Co., 1 Fed. 700; and other cases in note 96, supra.

An unauthorized attempt by a corporation to consolidate with another corporation by transferring all its property and franchises does not operate as a dissolution. Topeka Paper Co. v. Oklahoma Publishing Co., 7 Okla. 220.

99 In re Belton, 47 La. Ann.

100 Lane v. Bank of Tennessee,

was completed, in accordance with the contract and the provisions of its charter, and that it could therefore maintain the action.101

A corporation is not necessarily dissolved by a sale of all its property under execution, or on foreclosure of a mortgage. 102 Nor is it dissolved by the fact that all its property is held in the custody of a court of equity for the purpose of enforcing satisfaction of claims against it. 103

As was shown in another section, however, if all the property and franchises of a corporation are transferred by it under legislative authority, or sold, under legislative authority, on execution against it, or under a decree of foreclosure of a mortgage, or a decree to enforce a statutory lien of the state, there is, in effect, a surrender of its charter by the corporation with the consent of the state, and it is dissolved, unless its existence as a corporation is continued under the statutes, as is sometimes the case.104

# § 311. Insolvency-Appointment of receiver-Bankruptcy proceedings-Assignment.

The insolvency of a corporation, as we shall hereafter see, may be a cause for its dissolution in proper judicial proceedings, 105 but, since a corporation may exist without any assets at all, it necessarily follows that it is not dissolved by the mere fact that it is insolvent, and unable to pay its

note 87.

103 The fact that the property 83 Mo. 617. and most of the franchises of a 104 See an corporation are held in custody by there cited. a court of equity, for the purpose

Town of Westport, 39 Conn. 337. v. of enforcing satisfaction of specific claims against them, does not work Town of Westport, 39 Conn. 337.

102 Brinckerhoff v. Brown, 7

Johns. Ch. (N. Y.) 217; Smith v. franchise, and the corporation Gower, 2 Duv. (Ky.) 17; Gulf, Colorado & Santa Fe Ry. Co. v. personam on all causes of action Newell, 73 Tex. 334, 15 Am. St. for which it may be or become Rep. 788. Compare Slee v. Bloom, liable, without obtaining a license 19 Johns. (N. Y.) 456, 10 Am. Dec. 273, as to which, see ante, § 309, precedent to such actions. Heath v. Missouri Kansas & T. Ry. Co. v. Missouri, Kansas & T. Ry. Co.,

104 See ante, § 308, and the cases

105 Post, § 314(h).

debts, 106 unless it is expressly so provided by some statute. 107 Nor is a corporation dissolved by statutory proceedings in bankruptcy or insolvency, whether voluntary or involuntary, 108 or by the appointment of a receiver by a court of equity, 109 or by an assignment for the benefit of creditors. 110 A national bank

son v. New York Silk Mfg. Co., 11 Fed. 532; Adams v. Kehlor Milling Co., 35 Fed. 433; Davis v. Memphis & Charleston R. Co., 87 Ala. 633; Breene v. Merchants' & Mechanics' Bank, 11 Colo. 97; United States Electric Lighting Co. v. Leiter, 19 D. C. 575; City Ins. Co. of Providence v. Commercial Bank of Bristol, 68 Ill. 348; De Camp v. Alward, 52 Ind. 468; Valley Bank & Savings Institution v. Ladies' Congregational Sewing Society, Congregational Sewing Society, 28 Kan. 423; Boston Glass Manufactory v. Langdon, 24 Pick. (Mass.) 49, 35 Am. Dec. 292, 2 Smith's Cas. 604, 1 Cum. Cas. 478; Coburn v. Boston Papier Mache Mfg. Co., 10 Gray (Mass.) 243; Taylor v. Columbian Ins. Co., 14 Allen (Mass.) 353; Chamberlin v. Huguent Mfg. Co. 118 Mass. Huguenot Mfg. Co., 118 Massa 522; State v. Commercial Bank of Manchester, 13 Smedes & M. (Miss.) 569, 53 Am. Dec. 106; Parsons v. Eureka Powder Works, 48 N. H. 66; New Jersey Southern R. Co. v. Board of Railroad Commissioners, 41 N. J. Law, 235; Bradt v. Benedict, 17 N. Y. 93; Jackson v. McInnis, 33 Or. 529, 72 Am. St. Rep. 755; In re Worsted Mills, 9 Montg. Co. Law Rep. (Pa.) 23; Moseby v. Burrow, 52 Tex. 396; Dewey v. St. Albans Trust Co., 60 Vt. 1, 6 Am. St. Rep. 84; Shenandoah Valley R. Co. v. Griffith, 76 Va. 913; Sleeper v. Goodwin, 67 Wis. 577; Stolze v. Manitowoc Terminal Co., 100 Wis. 208. Compare State Savings Ass'n v. Kellogg, 52 Mo. 583; Briggs v. Penniman, 8 Cow. (N. Y.) 387, 18 Am. Dec. 454.

<sup>107</sup> Sprague-Brimmer Mfg. Co. v.

corporation remaining insolvent Manchester, 13 Smedes & M.

106 Second Nat. Bank of Pater- for one year shall be adjudged to be dissolved, insolvency for a year does not ipso facto dissolve a corporation, but there must be judicial proceedings, and a judgment of forfeiture. Stolze Manitowoc Terminal Co., 100 Wis.

> 108 Chamberlin v. Huguenot Mfg. Co., 118 Mass. 532; Coburn v. Boston Papier Mache Co., 10 Gray (Mass.) 243; Exchange Bank of Columbia v. Tiddy, 67 N. C. 169. Compare State Savings Ass'n v. Kellogg, 52 Mo. 583.

109 Taylor v. Columbian Ins. Co., 14 Allen (Mass.) 353; Bank of Bethel v. Pahquioque Bank, 14 Wall. (U. S.) 383; Central Nat. Bank of Baltimore v. Connecticut Bank of Baltimore v. Connecticut Mutual Life Ins. Co., 104 U. S. 54; State v. Butler, 86 Tenn. 614; Ordway v. Central Nat. Bank of Baltimore, 47 Md. 217; Moseby v. Burrow, 52 Tex. 396; Jackson v. McInnis, 33 Or. 529, 72 Am. St. Rep. 755; Kincaid v. Dwinelle, 59 N. Y. 548; City Insurance Co. of Providence v. Commercial Bank of Bristol, 68 Ill. 348; Montgomery v. Merrill, 18 Mich. 338; Heath v. Missouri, Kansas & T. Ry. Co., 83 Mo. 617; Rosenbaum v. United Mo. 617; Rosenbaum v. United States Credit System Co., 61 N. J. Law, 543; Jones v. Bank of Lead-ville, 10 Colo. 464; Exchange Bank of Columbia v. Tiddy, 67 N. C. 169; Steinhauer v. Colmar, 11 Colo. App. 494; State v. District Court, 22 Mont. 220; Stolze v. Manitowoc Terminal Co., 100 Wis. 208.

110 Boston Glass Manufactory v. Langdon, 24 Pick. (Mass.) 49, 35 Am. Dec. 292, 2 Smith's Cas. 604, 1 Cum. Cas. 478; De Camp v. Al-M. J. Murphy Furnishing Goods ward, 52 Ind. 468; Town v. Bank Co., 26 Fed. 572.

Where a statute provides that a 530; State v. Commercial Bank of is not dissolved by the fact that it is in the course of voluntary liquidation under the national banking act, and it may still sue and be sued.111

- II. FORFEITURE OF CHARTER AND FRANCHISES IN JUDICIAL PROCEEDINGS BY THE STATE.
- § 312. In general.—A corporation may forfeit its charter for misuser or nonuser, or for failure to perform conditions subsequent prescribed by its charter; but, as a rule, before the forfeiture can take effect, it must be judicially determined and declared in direct proceedings by or on behalf of the state.

A cause of forfeiture may be waived by the state, either expressly or impliedly, but an act of the legislature, to operate as a waiver, must not be consistent with an intention to afterwards enforce a forfeiture.

The fact that the state has violated its contract with a corporation does not bar a proceeding to forfeit its charter.

Another mode in which a corporation may be dissolved is by the forfeiture of its charter for misuser or nonuser of its franchises, or for failure to perform prescribed conditions subsequent, when the forfeiture has been judicially determined and decreed in proper proceedings by the attorney or solicitor general on behalf of the state. As was said by Mr. Justice Story in the supreme court of the United States, "a private corporation created by the legislature may lose its franchises by a misuser or a nonuser of them, and they may be resumed by the government under a judicial judgment upon a quo warranto to ascertain and enforce the forfeiture. This is the common law of the land, and is a tacit condition annexed to the creation of every such corporation."112 As we shall see in the follow-

(Miss.) 569, 53 Am. Dec. 106; State Bethel v. Pahquioque Bank, 14 Wall. (Md.) 205; Weyeth Hardware Mfg. Bank of Baltimore, 47 Md. 217. Co. v. James-Spencer-Bateman Co..

v. Bank of Maryland, 6 Gill & J. (U.S.) 383; Ordway v. Central Nat.

112 Terrett v. Taylor, 9 Cranch Co. v. James-Spencer-Bateman Co., 12 Terrett v. Taylor, 5 Granch 15 Utah, 110; Weigand v. Alliance Supply Co., 44 W. Va. 133. And see ante, \$ 310.

111 Central Nat. Bank of Balting Fig. 12. See, also, King v. Union Fire & Marine Ins. Co. of Newburyport, 5 Mass. 230, 4 Am. more v. Connecticut Mutual Life Dec. 50, I Smith's Cas. 375, I Cum. Ins. Co., 104 U. S. 54; Bank of Cas. 599; State v. Portland Nating sections, however, every act of misuser or nonuser is not necessarily sufficient ground for a judgment of forfeiture. Whether such a judgment will be rendered depends upon the circumstances.

## Necessity for judicial proceedings and judgment of forfeiture.

(a) In general.—When it is said that a corporation may forfeit its charter by misuser or nonuser of its franchises, it is not meant that the misuser or nonuser results ipso facto in its dissolution. On the contrary, as a general rule, however long a corporation may fail to exercise the powers conferred upon it, or however much it may abuse them, a forfeiture of its charter can only take effect upon a judgment of a competent tribunal in judicial proceedings instituted by authority of the state. The state may waive the forfeiture, 113 and until it institutes proceedings to have a forfeiture judicially determined and declared, and a judgment or decree of forfeiture is rendered, the existence of the corporation continues for all purposes, just as if there had been no misuser or nonuser; and the forfeiture cannot be set up collaterally by private individuals or other

ural Gas & Oil Co., 153 Ind. 483, ple, 166 Ill. 171; Com. v. Commer-74 Am. St. Rep. 314; State v. cial Bank, 28 Pa. St. 383; State Oberlin Building & Loan Ass'n, v. Cannon River Manufacturers' 35 Ohio St. 258, 1 Smith's Cas. Ass'n, 67 Minn. 14; and other 375, 1 Cum. Cas. 566; New York & cases more specifically cited in the Long Island Bridge Co. v. Smith, notes following. 148 N. Y. 540, 1 Smith's Cas. 367; People v. Utica Ins. Co., 15 Johns. (N. Y.) 358, 8 Am. Dec. 243; People v. North River Sugar Refining ple V. North River Sugar Remains Co., 121 N. Y. 582, 18 Am. St. Rep. 843, 2 Smith's Cas. 943, 1 Cum. Cas. 570; State v. Real Estate Bank, 5 Ark. 595, 41 Am. Dec. 109; Chesapeake & Ohio Canal Co. v. Baltimore & Ohio R. Co., 4 Gill & J. (Md.) 1; People v. Kingston & Middletown Turnpike Road Co., 23 Wend. (N. Y.) 193, 35 Am. Dec. 551; Henderson Loan & Real Estate American Loan & Real Estate Loan & Real Estat tate Ass'n v. People, 161 Ill. 196; Illinois Health University v. Peo-

For an extensive note on the forfeiture of corporate charters, in which many cases are collected, see 8 Am. St. Rep. 179 et seq.

Proceedings to forfeit the charter of a corporation for violation thereof are not precluded by a provision in its charter that it shall not be dissolved before the expiration of the period for which it was created, until all its debts are paid. State Bank v. State, Blackf. (Ind.) 267, 12 Am. Dec.

113 See post, § 315.

corporations, or even by the state, for the purpose of attacking the right of the corporation to exercise the powers and franchises conferred upon it by its charter.114

<sup>114</sup> Boston Glass Manufactory v. Langdon, 24 Pick. (Mass.) 49, 35 Am. Dec. 292, 2 Smith's Cas. 604, 1 Cum. Cas. 478; Heard v. Talbot, 7 Gray (Mass.) 113, 1 Smith's Cas. 358, 1 Cum. Cas. 482; Com. v. Union Fire & Marine Ins. Co., 5 Mass. 230, 4 Am. Dec. 50, 1 Smith's Cas. 369, 1 Cum. Cas. 599; State v. Fourth New Hampshire Turnpike, 15 N. H. 162, 41 Am. Dec. 690, 1 Smith's Cas. 390, 1 Cum. Cas. 593.

The following, among many other cases, are to the same effect:

England: King v. Amery, Term R. 515.

United States: Kanawha Coal Co. v. Kanawha & Ohio Coal Co., 7 Blatchf. 391, Fed. Cas. No. 7,606; County of Macon v. Shores, 97 U. S. 272, 277; Taylor v. Holmes, 14 Fed. 498.

Alabama: Duke v. Cahawba Nav. Co., 16 Ala. 372; Importing & Exporting Co. of Georgia v. Locke, 50 Ala. 332; Davis v. Memphis & Charleston R. Co., 87 Ala. 633; Hudgins v. State, 46 Ala. 208.

Arkansas: State v. Real Estate Bank, 5 Ark. 595, 41 Am. Dec. 109; Blackwell v. State, 36 Ark.

California: Union Water Co. v. Murphy's Flat Fluming Co., 22 Cal. 620.

Colorado: Humphreys v. Moo-

ney, 5 Colo. 282.

Connecticut: Kellogg v. Union Co., 12 Conn. 7; Pearce v. Olney, 20 Conn. 544; National Pahquioque Bank v. First Nat. Bank of Bethel, 36 Conn. 325, 4 Am. Rep. 80; New York & New England R. Co. v. New York, New Haven & H. R. Co., 52 Conn. 274.

Georgia: Union Branch R. Co. v. East Tennessee & Georgia R. Co., 14 Ga. 327; City of Atlanta v. Gate City Gas Light Co., 71 Ga.

106.

Illinois: Baker v. Backus, 32 III. 79; Mapes v. Scott, 94 III. 379;

Schools, 111 Ill, 171; Attorney General v. Chicago & Evanston R. Co., 112 Ill. 520.

Indiana: John v. Farmers' Mechanics' Bank, 2 Blackf. 367, 20 Am. Dec. 119; Brookville & Greensburg Turnpike Co. v. McCarty, 8 Ind. 392, 65 Am. Dec. 768; Barren Creek Ditching Co. v. Beck, 99 Ind.

Kentucky: Bank of Galliopolis

v. Trimble, 6 B. Mon. 599.

Louisiana: State v. Savings Bank, 31 La. Ann. 896; Bank of Louisiana v. Green, 20 La. Ann. 214.

Maine: Day v. Stetson, 8 Greenl. 365; Penobscot Boom Corp. v. Lamson, 16 Me. 224, 33 Am. Dec. 656.

Maryland: Chesapeake & Ohio Conal Co. v. Baltimore & Ohio R. Co., 4 Gill & J. 1; Laflin & Rand Powder Co. v. Sinsheimer, 46 Md. 315, 24 Am. Rep. 522.

Massachusetts: Briggs v. Cape Cod Ship Canal Co., 137 Mass. 71; Proprietors of Locks & Canals on Michigan: Toledo & Ann Arbor Lowell R. Co., 104 Mass. 1, 6 Am.

Rep. 181.

Michigan: Toledo & Ann. Arbor R. Co. v. Johnson, 49 Mich. 148; Cahill v. Kalamazoo Mut. Ins. Co., 2 Doug. 124, 43 Am. Dec. 457; Grand Rapids Bridge Co. v. Prange, 35 M<sup>†</sup> h. 400, 24 Am. Rep. 585.

Minnesota: Minnesota Central Ry. Co. v. Melvin, 21 Minn. 329.

Mississippi: Grand Gulf Bank v. Archer, 8 Smedes & M. 151; Arthur v. Commercial & Railroad Bank of Vicksburg, 9 Smedes & M. 394. 48 Am. Dec. 719; Bohannon v. Binns, 31 Miss. 355.

Missouri: Farmers' Bank Garten, 34 Mo. 119; Bank of Missouri v. Snelling, 35 Mo. 190.

New Hampshire: Sewall's Falls Bridge v. Fisk, 23 N. H. 171.

New Jersey. Jersey City Gaslight Co. v. Consumers' Gas Co., 40 People v. Board of Trustees of N. J. Eq. 427; New Jersey South-

For this reason, it was held in a leading Massachusetts case that a corporation created for the purpose of constructing and maintaining a canal, and authorized by its charter to maintain a dam for the purpose of supplying its canal with water, did not forfeit its charter or lose the right to maintain the dam. merely because it had ceased to use the canal for several years, and had filled up portions of it, and suffered it to remain in such a condition as to be entirely unfit for use, where there had been no surrender of its charter and acceptance thereof by the state, nor any judgment of forfeiture in proper judicial proceedings; and that the abandonment of the canal as a cause of forfeiture could not be set up collaterally by a private individual for the

39 N. J. Law, 28.

New York: People v. Hillsdale & Chatham Turnpike Road, 23 Wend. 254; Trustees of Vernon Society v. Hills, 6 Cow. 23, 16 Am. Society V. Hills, 6 Cow. 23, 16 Am. Dec. 429; Mickles v. Rochester City Bank, 11 Paige, 118, 42 Am. Dec. 103; Kincaid v. Dwinelle, 59 N. Y. 548; In re New York Elevated R. Co., 70 N. Y. 327; Denike v. New York & Rosendale Lime & Cement Co., 80 N. Y. 599; Clancey v. Onondaga Fine Salt Mfg. Co., 62 Raph, 295. Ormsby v. Verment Barb. 395; Ormsby v. Vermont Copper Min. Co., 65 Barb. 360; Boyer v. Village of Little Falls, 5 App. Div. 1; People v. Ulster & Delaware R. Co., 128 N. Y. 240 (affirming 58 Hun, 266).

North Carolina: Asheville Division No. 15, Sons of Temperance,

v. Aston, 92 N. C. 578. Ohio: Receivers of Bank of Circleville v. Renick, 15 Ohio, 322; Johnson v. Bentley, 16 Ohio, 97. Oregon: Oregon Cascade R. Co.

v. Baily, 3 Or. 164.

Pennsylvania: Centre & Kishacoquillas Turnpike Road Co. v. Mc-Conaby, 16 Serg. & R. 140; Lehigh Bridge Co. v. Lehigh Coal & Navigation Co., 4 Rawle, 8, 26 Am. Dec. 111; Forster v. Juniata Bridge Co., 16 Pa. St. 393; Cleveland & Pittsburg R. Co. v. Speer, 56 Pa. St. 325, 94 Am. Dec. 84; Hanover

ern R. Co. v. Long Branch Com'rs, Junction & Susquehanna R. Co. v. Grubb, 82 Pa. St. 36; In re Philadelphia & Merion Ry. Co., 187 Pa. St. 123.

> South Carolina: Shand v. Gage, 9 Rich. 187; State v. Spartanburg Clifton & G. R. Co., 51 S. C. 129.

> Tennessee: State v. Butler, 15 Lea, 104; Bache v. Nashville Horticultural Soc., 10 Lea, 436.

> Moseby v. Burrow, 52 Texas: Tex. 396.

> Virginia: Bank of Virginia v. Poitiaux, 3 Rand. 136, 15 Am. Dec. 706; Crump v. United States Mining Co., 7 Grat. 352, 56 Am. Dec. 116; Pixley v. Roanoke Navigation Co., 75 Va. 320.

> West Virginia: Greenbrier Lumber Co. v. Ward, 30 W. Va. 43; Moore v. Schoppert, 22 W. Va. 282.

> Wisconsin: Attorney General v. Chicago & North Western Ry. Co., 35 Wis. 425; Attorney General v. Superior & St. Croix R. Co., 93 Wis. 604.

> Under a statute declaring that, whenever a corporation shall have remained insolvent for one year, it shall be adjudged to be dissolved, such insolvency does not ipso facto operate as a dissolution, but judicial proceedings and a judgment of forfeiture are necessary. Stolze v. Manitowoc Terminal Co., 100 Wis.

purpose of attacking the right of the company to maintain the dam.

It was said by Judge Bigelow in this case: "In the absence of express conditions in an act of incorporation, by which corporate rights and powers are made to depend on their due exercise, a nonuser or misuser of them does not operate as a surrender or forfeiture of the charter. Although the disuse of the canal and its abandonment by the corporation may be a gross disregard of the duty imposed on them by law, and an essential violation of the terms and conditions implied from the contract entered into with the government by the acceptance of the charter, and, upon due proceedings had, might be a sufficient ground upon which to decree a forfeiture of all their corporate rights and privileges, they do not constitute any valid ground upon which the exercise by the corporation of any of the powers conferred by their charter can be defeated or denied by third persons in collateral proceedings. This results from the very nature of an act of incorporation. It is not a contract between the corporate body, on the one hand, and individuals whose rights and interests may be affected by the exercise of its powers, on the other. It is a compact between the corporation and the government from which they derive their powers. dividuals therefore cannot take it upon themselves in the assertion of private rights, to insist on breaches of the contract by the corporation, as a ground for resisting or denying the exercise of a corporate power. That can be done only by the government with which the contract was made, and in proceedings duly instituted against the corporation. It would not only be a great anomaly to allow persons, not parties to a contract, to insist on its breach and enforce a penalty for its violation; but it would be against public policy, and lead to confusion of rights, if corporate powers and privileges could be disputed and defeated by every person, who might be aggrieved by their exercise. Therefore it has been often held, that a cause of forfeiture, however great, cannot be taken advantage of or enforced against corporations collaterally or incidentally, or in any other mode than by a direct proceeding for that object in behalf of the government."115

(b) Nonperformance of conditions subsequent expressed in charter.—What has been said in the preceding paragraphs also applies, as a general rule, when a corporation fails to comply with conditions subsequent expressed in its charter, even though the charter may declare the penalty of forfeiture for failure to comply therewith. As we have seen in another section, it is competent for the legislature to provide in the charter of a corporation that it shall cease to exist if it shall fail to comply with a prescribed condition subsequent, and if such an intention on the part of the legislature clearly appears, failure to comply with the conditions will result, ipso facto, in a forfeiture of the charter and a dissolution of the corporation, without any judicial proceedings. 116 Ordinarily, however, failure of a corporation to comply with a condition subsequent imposed by its charter is merely a cause of forfeiture in proper proceedings on behalf of the state brought directly for that purpose, and cannot be set up collaterally either by private individuals or other corporations, or by the state. 117

Cum. Cas. 482.

116 See ante, § 306.

117 United States: Wallamet Falls Canal & Lock Co. v. Kittridge, 5 Sawy. 44, Fed. Cas. No. 17,105, 1 Smid's Cas. 362; Frost's Lessee v. Frostburg Coal Co., 24 How. 283; Davis v. Gray, 16 Wall. 203; Hughes v. Northern Pacific Ry. Co., 18 Fed. 106; Hyde v. Doe, 4 Sawy. 133, Fed. Cas. No. 6,969.

California: Mokelumne Hill Canal & Mining Co. v. Woodbury, 14 Cal. 424, 73 Am. Dec. 658; Santa Rosa City R. Co. v. Central Street Ry. Co., 38 Pac. 986; People v. Los Angeles Electric Ry. Co., 91 Cal. 338.

Connecticut: Enfield Toll Bridge Co. v. Connecticut River Co., 7

Conn. 28.

Illinois: Cross v. Pinckneyville

115 Heard v. Talbot, 7 Gray kakee River Improvement Co., 103 (Mass.) 113, 1 Smith's Cas. 358, 1 Ill. 491, 1 Smith's Cas. 377; People v. National Savings Bank, 129 Ill.

> Louisiana: Wright v. Benjamin, 5 La. Ann. 179; State v. Fagan, 22 La. Ann. 545.

> Maine: Bear Camp River Co. v. Woodman, 2 Me. 404.

Maryland: Chesapeake & Ohio Canal Co. v. Baltimore & Ohio R. Co., 4 Gill & J. 1; Lord v. Essex Building Ass'n, 37 Md. 320.

Massachusetts: Com. v. Tenth Massachusetts Turnpike Corp., 11 Cush. 171; Briggs v. Cape Cod Ship Canal Co., 137 Mass. 71; Mer-rick v. Reynolds Engine & Governor Co., 101 Mass. 381.

Missouri: St. Joseph & Iowa R. Co. v. Shambaugh, 106 Mo. 557,

New Hampshire: State v. Fourth Mill Co., 17 Ill. 54; People v. Kan- New Hampshire Turnpike, 15 N.

An intention on the part of the legislature that the failure of a corporation to comply with a condition subsequent shall ipso facto dissolve the corporation, instead of being merely a cause of forfeiture in direct proceedings by the state, will not be implied from language which will reasonably admit of a different construction, for it is not only the better policy to allow no one but the state to object to a corporation's failure to comply with conditions prescribed in its charter, but is also more in accord with justice, and with legal principles, to require legal proceedings by the state, in which the corporation may have a hearing, for the purpose of determining judicially whether the conditions prescribed in the charter have been complied with or not.118 Therefore, where charters or general laws have required corporations to comply with certain conditions subsequent, and have declared merely that, on failure to do so, they should be "dissolved," or that their charters should be "forfeited," etc., it has been held that this meant merely that they should be liable to forfeiture and dissolution in proper judicial proceedings by authority of the state, and on judgment of forfeiture, and not that they should be dissolved or lose the

H. 162, 41 Am. Dec. 690, 1 Smith's Co. v. Vermont Central R. Co., 34 Cas. 370, 1 Cum. Cas. 593. Vt. 1.

Cas. 370, 1 Cum. Cas. 593.

New York: New York & Long Island Bridge Co. v. Smith, 148 N. Y. 540, 1 Smith's Cas. 367; In re King's County Elevated R. Co., 105 N. Y. 97; Day v. Odgensburgh & Lake Champlain R. Co., 107 N. Y. 129; People v. Buffalo Stone & Cement Co., 131 N. Y. 140; People v. Manhattan Co., 9 Wend. 382; Bradt v. Benedict, 17 N. Y. 93; Mickles v. Rochester City Bank, 11 Paige, 118, 42 Am. Dec. 103. Paige, 118, 42 Am. Dec. 103.

South Carolina: State v. Spartanburg, Clifton & G. R. Co., 51 S.

Tennessee: State v. Nonconnah Turnpike Co., 1 Tenn. Cas. 511.

Texas: City of Houston v. Houston, Belt & M. P. Ry. Co., 84 Tex. 581.

Vermont: Vermont & Canada R. attorney general."

West Virginia: Greenbrier Lumber Co. v. Ward, 30 W. Va. 43.

Wisconsin: Harrod v. Hamer, 32 Wis. 162; Attorney General v. Superior & St. Croix R. Co., 93 Wis. 604.

As to the distinction between conditions subsequent and conditions precedent to acquiring corporate existence, see ante, § 73.

<sup>148</sup> See New York & Long Island Bridge Co. v. Smith, 148 N. Y. 540, 1 Smith's Cas. 367, where it was said by Judge Bartlett that "it requires, however, strong and unmistakable language \* \* \* to authorize the court to hold that it was the intention of the legislature to dispense with judicial proceedings on the intervention of the rights and franchises conferred by their charters, ipso facto, by the mere failure to comply with the conditions.119

In a federal case, in which a statute provided that if any corporation organized thereunder should, for any period of six months after the commencement of its business, neglect and cease to carry on the same, "its corporate powers should also cease," Judge Deady held that this language was equivalent to saying that "its corporate powers should be forfeited," that the statute was not self-executing, but contemplated a judicial proceeding to determine and enforce the forfeiture, and that, if there had been a failure to comply with the condition, no one could allege it or take advantage of it but the state. "In this respect," he said, "a corporation is like an estate in fee. If a condition subsequent is annexed to such an estate, no one but the grantor or his successors can take advantage of its nonperformance."120

In a late New York case, where the act incorporating a bridge company provided that if the bridge should not be commenced within two years, the "act and all rights and privileges granted" thereby should be "null and void," it was held that the provision was not self-executing, and that failure to commence the bridge within two years did not ipso facto dissolve the cor-

Co. v. Kittridge, 5 Sawy. 44, Fed. Cas. No. 17,105, 1 Smith's Cas. 362; People v. Kankakee River Improvement Co., 103 Ill. 491, 1 Smith's Cas. 377; New York & Long Island Bridge Co. v. Smith. 148 N. Y. 540, 1 Smith's Cas. 367; State v. Fourth New Hampshire Turnpike, 15 N. H. 162, 41 Am. Dec. 690, 1 Smith's Cas. 370, 1 Cum. Cas. 593; Attorney General v. Superior & St. Croix R. Co., 93 Wis. 604; Vermont & Canada R. Co. v. Vermont Central R. Co., 34 Vt. 2; People, v. Los Angeles Electric Ry. Co., 91 Cal. 338; and other cases cited in note 117, supra, a number of which are to the same effect.

119 Wallamet Falls Canal & Lock Independence S. L. R. Co., 52 Mo. App. 439.

> 120 Wallamet Falls Canal & Lock Co. v. Kittridge, 5 Sawy. 44, Fed. Cas. No. 17,105, 1 Smith's Cas. 362.

So, in Frost's Lessee v. Frostburg Coal Co., 24 How. (U. S.) 283, where a statute provided that, if four-fifths of the capital stock of a corporation should become concentrated in the hands of less than five persons, "the corporate powers and privileges should cease and determine," it was held that the happening of such a contingency was a cause of forfeiture of which a private party could not take adof which are to the same effect. vantage. The court said: "That Compare Ford v. Kansas City & is a question for the sovereign

poration.<sup>121</sup> And a like construction has been placed upon a statute or charter providing that, if a railroad company should fail to construct its road within a certain time, all rights, privileges, and immunities granted thereby should "cease and be void."122

(c) Power of governor.—Since judicial proceedings at the instance of the state are necessary to enforce a forfeiture of the charter of a corporation for misuser or abuse or nonuser of its franchises, or for neglect of duty to the public, the governor of a state has no power to enforce a forfeiture and dissolve a corporation by proclamation. It was so held where a military governor, in charge of one of the southern states during the reconstruction period by appointment of the federal government, undertook to dissolve a corporation by proclamation. 123

## § 314. Grounds for forfeiture of charter.

(a) In general.—When a corporation has been guilty of acts or omissions of duty which, by its charter or some other statute, are made a cause of forfeiture of its franchise to be a corporation, and proceedings are instituted on behalf of the state to enforce the forfeiture, the court has no discretion to refuse a judgment of forfeiture. 124 But in other cases, where a corporation has merely violated its charter by doing unau-

force it at its pleasure."

121 New York & Long Island Bridge Co. v. Smith, 148 N. Y. 540, 1 Smith's Cas. 367.

122 State v. Spartanburg, Clifton & G. R. Co., 51 S. C. 129.

123 Shand v. Gage, 9 S. C. 187.

124 State v. Oberlin Building & Loan Ass'n, 35 Ohio St. 258, 1 Smith's Cas. 362; Frost's Lessee

power, which may waive it or en- 129 Ill. 618; State v. Southern Pacific R. Co., 24 Tex. 80.

Thus in People v. Buffalo Stone & Cement Co., 131 N. Y. 140, where a statute provided that the capital stock of corporations formed thereunder should be paid in, one-half in one year, and the other half in two years, from the incorporation, and declared that, in default thereof, the corporation should be dissolved, it was held that the statute State v. Pennsylvania & Ohio Canal Co., 23 Ohio St. 121; People v. ceedings by the attorney general Kankakee River Improvement Co., to dissolve a corporation for fail-103 III. 491, 1 Smith's Cas. 377; ure to comply with the statute, People v. Buffalo Stone & Cement the court, on proof that the statute Co., 131 N. Y. 140; People v. City had not been complied with, had Bank of Leadville, 7 Colo. 226; no discretion to refuse a decree People v. National Savings Bank, of dissolution. thorized acts, or where it has been guilty of neglect, the court is vested with a discretion to determine whether judgment of ouster of the franchise to be a corporation shall be rendered, or whether the corporation shall merely be ousted from the exercise of the powers illegally assumed, or required to perform the duties neglected; and in determining this question it will consider both the interests and welfare of the public and the interests of stockholders and of creditors. 125

In an Ohio case, an incorporated building and loan association had been guilty of habitual violation of its charter by refusing to loan its funds to its members, and conducting its business in such a way as to prevent such loans, by making loans to persons who were not members, by borrowing money for the purpose of lending it, by dividing money and securities among certain stockholders, and by trafficking in shares of its own stock. A majority of the court, in view of the fact that. if the corporation was permitted to wind up its affairs, the work would be accomplished in a few months, but, if it should be ousted from its franchise to be a corporation, trustees would have to be appointed under the statute, which would occasion delay and involve increased expense, held, though "with some hesitation," that it would be "for the interest of the stockholders, as well as the public," to render a judgment of ouster, not from the franchise to be a corporation, but merely from the exercise of the powers illegally assumed, and such a judgment was rendered. The chief justice dissented, being of the opinion that such flagrant and persistent violations of corporate powers called for and required an application of the severest penalties of the law, and that the judgment should oust the defendant from the franchise of being a corporation. 126

<sup>125</sup> State v. Oberlin Building & Vt. 489; People v. Ulster & Dela-Loan Ass'n, 35 Ohio St. 258, 1 ware R. Co., 128 N. Y. 240; State Smith's Cas. 375, 1 Cum. Cas. 566. v. Farmers' College, 32 Ohio St. See, also, State v. Standard Oil Co., 487; State v. Pawtuxet Turnpike 49 Ohio St. 137, 34 Am. St. Rep. Corp., 8 R. I. 182, 521, 94 Am. Dec. 541; State v. Portland Natural Gas & Oil Co., 153 Ind. 483, 74 Am. St. in the sections following.

Rep. 314; State v. Essex Bank, 8

As a general rule, the charter of a corporation will not be forfeited for misuser, or for nonuser or neglect, unless it was willful or fraudulent, or at least due to culpable negligence, or unless the legislature has expressly prescribed the penalty or forfeiture. "To work a forfeiture," said Judge Cowen in a New York case, "there should be something wrong; and not only a wrong, but one arising from willful abuse or improper neglect. An inability, through misfortune, to answer the design for which the body politic was instituted, is also a cause of forfeiture. That, however, is on a distinct reason, not so directly material, and of which it is not necessary to say much. The prosecution before us goes on corporate default, or corporate wrong, which must, I think, be more than accidental negligence, or a mere mistaken excess of power, or a mistake in the mode of exercising an acknowledged power. There must be an abuse of trust somewhat of such a nature as would render a trustee liable to forfeit his station, on the complaint of his cestui que trust, if the question stood on the relation between them. Corporations are political trustees. Have they fulfilled the purposes of their trust, or acted in good faith with a view to their fulfillment, is the question to be asked, when they are called on to forfeit their charter, either for acts of commission or omission; unless indeed they are so generally crippled and broken down in their affairs, as, in the judgment of a court and jury, to be incapable of prosecuting their business with safety to that community who granted the charter, and who hold the relation of cestui que trust."127 In some of the cases it has

Loan Ass'n, 35 Ohio St. 258, 1 Gill & J. (Md.) 365, 379, 31 Am. Smith's Cas. 375, 1 Cum. Cas. 566. Dec. 72; Harris v. Mississippi Val
127 People v. Bristol & Rensseley & Ship Island R. Co., 51 Miss. laerville Turnpike Road, 23 Wend. 602; State v. Societe Republicaine, (N. Y.) 222, 236. See, also, Pas- 6 Mo. App. 114; Thompson v. Peochall v. Whitsett, 11 Ala. 472; ple, 23 Wend. (N. Y.) 537; PeoState v. Real Estate Bank, 5 Ark. ple v. Kingston & Middleton Turn-State V. Real Estate Bank, 5 Ark. pie V. Ringston & Middleton Turn595, 41 Am. Dec. 109; City of Topike Road Co., 23 Wend. (N. Y.)
peka v. Topeka Water Co., 58 Kan. 193, 35 Am. Dec. 551; People v.
349; Chesapeake & Ohio Canal Atlantic Avenue R. Co., 125 N.
Co. v. Baltimore & Ohio R. Co., 4 Y. 513; Ward v. Sea Ins. Co., 7
Gill & J. (Md.) 1; Regents of University of Maryland v. Williams, 9 bana & Champaign Mutual Ins. been said that, to authorize a judgment of forfeiture for misuser, there must be "willful and repeated acts." 128

Even when the abuse of its franchises by a corporation, or its neglect of duty, is willful and fraudulent, the court will not necessarily give a judgment of forfeiture. In the first place. the abuse or neglect must be such as to affect the public, for, if it affects purely private interests only, there are other remedies. 129 "It appears to be settled," said Judge Finch in a New York case, "that the state as prosecutor must show on the part of the corporation accused some sin against the law of its being which has produced, or tends to produce, injury to the public. The transgression must not be merely formal or incidental, but material and serious; and such as to harm or menace the pub-For the state does not concern itself with the quarrels of private litigants. It furnishes for them sufficient courts and remedies, but intervenes as a party only where some public interest requires its action. Corporations may, and often do, exceed their authority where only private rights are

Co., 14 Ohio, 7; State v. Oberlin intentional or voluntary, or was Building & Loan Ass'n, 35 Ohio St. such neglect as to indicate an in-258, 1 Smith's Cas. 375, 1 Cum. Cas. difference to the demands of public 566; State v. People's Mutual Benduty, or was so material a disefit Ass'n, 42 Ohio St. 579; Com. v. obedience of law as, within estab-Allegheny Bridge Co., 20 Pa. St. lished rules, would warrant a judg-185; State v. Pawtuxet Turnpike ment of dissolution. Corp., 8 R. I. 182, 521, 94 Am. Dec.
123; State v. Merchants' Insurance tween corporations 123; State v. Merchants insurance & Trust Co., 8 Humph. (Tenn.) 235; State v. Rio Grande R. Co., 41 Tex. 217; State v. Royalton & Woodstock Turnpike Co., 11 Vt. 431; State v. Janesville Water Co., 92 Wis. 496.

128 State v. Societe Republicaine, 9 Mo. App. 114; State v. Council Bluffs & Nebraska Ferry Co., 11 Neb. 354.

In People v. Atlantic Avenue R. Co., 125 N. Y. 513, it was held that

An ultra vires consolidation between corporations is no ground for forfeiting their charters, where the consolidation has been declared void, and there has been no injury to the public, and where it was attempted in good faith and on the advice of counsel. State v. Crawfordsville & Shannondale Turnpike Co., 102 Ind. 283. See, also, Moore v. State, 71 Ind. 478.

Refining Co., 121 N. Y. 582, 18 Am. St. Rep. 843, 2 Smith's Cas. 943, 1 where an act or omission on the part of a corporation is not made part of a corporation is not made a cause of forfeiture by statute, Harris v. Mississippi Valley & irrespective of its intent or character, it cannot be made the basis of a proceeding to forfeit the charter of a corporation, unless it was v. Bogart, 45 Cal. 73.

affected. When these are adjusted, all mischief ends and all harm is averted. But when the transgression has a wider scope and threatens the welfare of the people, they may summon the offender to answer for the abuse of its franchise or the violation of its corporate duty."130

In the second place, as is shown above, though the misuser or nonuser of its franchises by a corporation may have been willful and fraudulent, the court may, on a consideration of the interests of the stockholders, as well as the public, oust the corporation from the exercise of the powers illegally assumed, instead of ousting it from the franchise to be a corporation. 131 To authorize a judgment of forfeiture, the misuser or nonuser must affect matters which are of the essence of the contract between the corporation and the state. 132

(b) Misuser or abuse of franchises in general.—As was shown in another paragraph, misuser or abuse of its franchises by a corporation is not ground for proceedings to forfeit its charter, unless such a penalty has been prescribed by the legislature, where the misuser or abuse was not willful or fraudulent. but was due to accident or to a bona fide mistake as to the pow-

In a late Indiana case it was said: "The authorities assert, as a general rule, that courts will proceed with extreme caution in the forfeiture of corporate franchises, and a corporation will not be deprived thereof unless under express limitation, or for a plain abuse of its powers, whereby it fails to fulfill the design and pur-pose of its organization. When the state seeks to destroy the life of an incorporate body, it is required

Renning Co., 121 N. Y. 582, 18 Am. adequate remedies are provided."
St. Rep. 843, 1 Cum. Cas. 570. See, State v. Portland Natural Gas & also, People v. Rosenstein Cohn Cigar Co. (Cal.) 63 Pac. 163.

In a late Indian. 130 People v. North River Sugar private interests for which other

131 See supra, this section, notes 125, 126,

182 Harris v. Mississippi Valley & Ship Island R. Co., 51 Miss. 602; State v. Council Bluffs & Nebraska Ferry Co., 11 Neb. 354.

"It is only for the violation of an express provision of the organic law under which a corporation derives its powers or privileges, or for such a misuse or nonuse of them as results in a substantial to show some grave misconduct, failure to fulfill the design and some act at least by which it has purpose of its organization, that a offended the law of its creation, forfeiture of a franchise will be or something material which tends to produce injury to the public, and not merely that which affects only 123, affirming 89 Fed. 235.

ers conferred by the charter. 133 Nor is willful or fraudulent misuser or abuse of its franchises a ground of forfeiture, in the absence of express statutory provision therefor, unless it is such as to affect or menace the interests or welfare of the public, 134 or, where it is alleged to consist in a violation of the charter of the corporation, unless it affects matters which are of the essence of the contract between the corporation and the state. 135

As a general rule, however, the charter of a private corporation will be forfeited, in proper proceedings by the state, for any willful or fraudulent misuser or abuse of its franchises which injures or menaces the interests or welfare of the state or of the community in which it transacts business, whether the misuser or abuse consists in the exercise of a franchise or power not conferred upon the corporation by its charter, or in the violation of prohibitions in its charter, or in the violation of prohibitions in general laws to which it is subject, or in the violation of established principles based upon the ground of public policy.136

For example, it has been held or said to be a ground of forfeiture for an insurance company to carry on the business of

133 Supra, this section (a).

134 Id.

135 Id.

136 Mississippi, Ouachita & Red River R. Co. v. Cross, 20 Ark. 443; Darnell v. State, 48 Ark. 321; Ward v. Farwell, 97 Ill. 593; People v. Chicago Gas Trust Co., 130 Ill. 268, 17 Am. St. Rep. 319; Dis-Orleans Gas Light & Banking Co., Stearns, 4 Cush. (Mass.) 60; State Ry. Co., 45 Wis. 579.

v. Equitable Loan & Inv. Ass'n, 142 Mo. 325; State v. Bacon Club of Neosho, 44 Mo. App. 86; State v. Nebraska Distilling Co., 29 Neb. 700; People v. Utica Ins. Co., 15 Johns. (N. Y.) 358, 8 Am. Dec. 243; People v. North River Sugar Refining Co., 121 N. Y. 582, 18 Am. St. Rep. 843, 2 Smith's Cas. 943, 1 Cum. Cas. 570; People v. Globe Mutual Life Ins. Co., 60 How. Pr. tilling & Cattle Feeding Co. v. Mutual Life Ins. Co., 60 How. Pr. People, 156 Ill. 448, 47 Am. St. Rep. (N. Y.) 82; State v. Hazleton & 200; Illinois Health University v. Leetonia Ry. Co., 40 Ohio St. 504; People, 166 Ill. 171; Bank of Vin-State v. Standard Oil Co., 49 Ohio cennes v. State, 1 Blackf. (Ind.) St. 147, 34 Am. St. Rep. 541; 267, 12 Am. Dec. 234; State v. New Trustees of McIntire Poor School v. Zanesville Canal & Mfg. Co., 9 Ohio Canal Co. v. Baltimore & v. Commercial Bank, 28 Pa. St. Ohio R. Co., 4 Gill & J. (Md.) 1; 383; State v. Southern Pacific R. Washington & Baltimore Turnpike Co., 24 Tex. 80; State v. Essex Road v. State, 19 Md. 239; State v. Bank, 8 Vt. 489; State v. Pasump-Easton Social, Literary & Musical sic Turnpike Co., 3 Vt. 178; State Club, 73 Md. 97; Lumbard v. v. Milwaukee, Lake Shore & W.

banking in violation of a general law prohibiting unauthorized banking;187 for a bank to willfully violate a prohibition in its charter against making loans and discounts at a greater rate than is prescribed, and in dealing in promissory notes otherwise than by discounting them; 138 for an insurance company to continue business and issue policies when its condition is such that it will not be able to pay losses; 139 for an insurance company to misappropriate its entire capital through the deliberate and fraudulent action of its trustees, and also a large sum received from policy holders in addition thereto. 140

It has also been held ground of forfeiture for a bank to contract debts or issue bills to a greater amount than is allowed by its charter, or to fraudulently issue more paper than it can redeem;141 for a bank to withdraw stock under the form of loans upon private security, with intent to reduce the effective capital below the amount required by its charter; 142 for a corporation to increase its capital stock without legislative sanction, or issue certificates of stock beyond the amount of the capital;143 or to willfully violate statutory or constitutional provisions as to the amount of subscriptions for stock before commencement of business, or as to payment for stock.\*

Johns. (N. Y.) 358, 8 Am. Dec. 243. 138 Com. v. Commercial Bank, 28 Pa. St. 383.

139 Ward v. Farwell, 97 Ill. 593.

140 People v. Globe Mutual Life Ins. Co., 60 How. Pr. (N. Y.) 82 (under a statute providing that a corporation may be annulled whenever it offends against the provisions of the act creating it).

141 Bank of Vincennes v. State, 1 Blackf. (Ind.) 267, 12 Am. Dec. 234.

142 State v. Essex Bank, 8 Vt.

143 People v. Parker Vein Coal Co., 10 How. Pr. (N. Y.) 543.

\*The charter of a corporation may be forfeited for failure to comply with a statute requiring its full

137 People v. Utica Ins. Co., 15 one year from the date of its organization. People v. City Bank of Leadville, 7 Colo. 226.

Failure to comply with a constitutional provision that no corporation shall issue stock or bonds except for labor done or money or property actually received, and a charter provision that no stock shall be issued or certificate given therefor until the amount sub-scribed for has been fully paid renders the corporation subject to forfeiture. State v. New Orleans De-benture Redemption Co., 51 La. Ann. 1827.

When the charter of a corporation authorizes it to commence business only when one thousand shares of its stock have been subscribed, commencement of business when only a few hundred shares capital stock to be paid up within have been subscribed is ground for

And it has been held cause for forfeiture for a turnpike company to place its toll gate in an unauthorized place;144 or to collect tolls before performance of prescribed conditions precedent, or to collect excessive tolls; 145 for a corporation to enter into an unauthorized and unlawful combination with other corporations, or with corporations and natural persons, for the purpose of preventing competition and creating a monopoly. 146

State v. Debenture Guarantee & 267, 45 Am. St. Rep. 609. Loan Co., 51 La. Ann. 1874.

Co., 3 Vt. 178.

145 People v. Kingston & Middletown Turnpike Road Co., 23 Wend. (N. Y.) 193, 35 Am. Dec. 551.

Cum. Cas. 570; People v. Milk Exchange, 145 N. Y. 267, 45 Am. St. Rep. 609; State v. Standard Oil Co., 49 Ohio St. 137, 34 Am. St. Rep. 541; State v. Portland Natural Gas & Oil Co., 153 Ind. 483, Cattle Feeding Co. v. People, 156 land Natural Gas & Oil Co., 153 Ill. 448, 47 Am. St. Rep. 200; Peo- Ind. 483, 74 Am. St. Rep. 314. ple v. Chicago Gas Trust Co., 130

laws declaring that its directors ing its stock. should have the power to make corporation, and, acting under tered into an illegal trust agree-such by-laws, the directors from ment with other corporations and milk to be paid by dealers, and that if a corporation becomes an the price so fixed largely con-integral part of a combination trolled the market in and about which possesses over it absolute the city in which the corporation control, which has absorbed most held that these facts supported a tates the extent, manner, and verdict or finding that the corpo- terms of its entire business acration as thus managed constituted tivity; if that combination draws a combination inimical to trade under its control other corporaand commerce, and therefore un-tions in the same business; if all lawful and were sufficient to sus- the stock is transferred to a cen-

proceedings to forfeit its charter, ple v. Milk Exchange, 145 N. Y.

Where two corporations created 144 State v. Pasumpsic Turnpike for the purpose of supplying natural gas to the people of a city entered into an agreement fixing the price of gas to be charged to consumers, and stipulating that 146 People v. North River Sugar neither would furnish gas to per-Refining Co., 121 N. Y. 582, 18 Am. sons who were patrons of the other. St. Rep. 843, 2 Smith's Cas. 943, 1 it was held that the agreement was unlawful as a restraint upon competition between panier, and as tending to create a monopoly, and that it might be made the basis of proceedings in quo warranto by the state to for-74 Am. St. Rep. 314; Distilling & feit their charters. State v. Port-

See, also, People v. Chicago Gas Ill. 268, 17 Am. St. Rep. 319; State Trust Co., 130 Ill. 268, 17 Am. St. v. Nebraska Distilling Co., 29 Neb. Rep. 319, where a gas company obtained control of another gas com-Where a corporation adopted by- pany in the same city by purchas-

In a late New York case, in and fix the standard or market which the charter of the North price at which milk should be pur- River Sugar Refining Company chased by the stockholders of the was forfeited because it had entime to time fixed the price of persons, it was held in substance had its place of business, it was of its corporate functions, and dictain a judgment forfeiting the tral board, and in exchange for it charter of the corporation. Peo- certificates are taken and distrib-

Where a railroad company failed to construct the line provided for in its charter, but condemned private property, and constructed a road wholly unsuited to the wants of the public, and for the benefit only of mines owned by the principal stockholders of the company, it was held an abuse and misuser of its corporate powers for which it might be dissolved in proceedings by the state.147 Other cases are referred to in the note below.\*

uted to its own stockholders, carrying a proportionate interest in what it describes as its capital stock, new directors being chosen by the board, who are made eligible by the gift to them of single shares, and liable to be removed under the terms of their appointment at any moment of independent action; if it loses its power to make a dividend, and is compelled to pay over its net earnings to a master whose servant it has become, and ceases to carry on business under orders of that master, cannot stir without his approval, and yet is entitled to receive from the earnings of the other corporations its proportion-ate share of all profits, for division among its own stockholders, who hold substituted certificates, and is liable to be mortgaged, not for its own corporate benefit alone, but to supply with funds the controllin : board when reaching out for other coveted corporations and their business,-such corporation has been guilty of an excess and abuse of its power which threatens and harms the public welfare, and justifies a judgment of dissolution. People v. North River Sugar Refining Co., 121 N. Y. 582, 18 Am. St. Rep. 843, 2 Smith's Cas. 943, 1 Cum. Cas. 570.

See, also, State v. Standard Oil Co., 49 Ohio St. 137, 34 Am. St. Rep. 541, where a combination or trust was formed between oil companies by transfer of stock to trus-

147 State v. Hazelton & Leetonia Ry. Co., 40 Ohio St. 504.

lege may be forfeited where it appears that it is conducted for pecuniary profit, and confers degrees and issues diplomas for a price, without regard to the qualification, of the applicant to practice medicine, and sometimes without any examination at all. Independent Medical College v. People, 182 Ill. 274; Illinois Health University v. People, 166 Ill. 171.

Where a debenture redemption company exposes the public with whom it deals to inevitable loss because its plan is not feasible, the state may annul the charter. State v. New Orleans Debenture Redemption Co., 51 La. Ann. 1827; State v. Louisiana Debenture Co., 51 La. Ann. 1795; State v. Debenture Guarantee & Loan Co., 51 La. Ann.

The state is not prevented from instituting proceedings to annul the charter of a corporation on the ground that the business, because of the plan upon which it is carried on, will inevitably injure and defraud the public dealing with it, by the fact that a statute allows corporations to be organized for carrying on "any lawful business." and that the legislature has not declared unlawful the business for which the corporation was organ-State v. Debenture Guarantee & Loan Co., 51 La. Ann. 1874.

The fact that a license has been issued to a corporation does not estop the state from instituting proceedings to forfeit its charter because its objects are not feasible, or not in accordance with the pol-The charter of a medical col- icy of the state. State v. New Or-

On the other hand, it has been held not to be a ground of forfeiture for corporations to enter into an ultra vires consolidation, where they act in good faith, and the consolidation is afterwards declared void; 148 for a corporation authorized by its charter to loan money, without any express restriction as to the rate of interest, to make loans at usurious rates; 149 for a railroad company to obtain a charter from another state; 150 for a corporation to use an abbreviation of its corporate name;151 or to have no sign at its office, and to fail to list its property for taxation: 152 for a turnpike company to commit a trespass in constructing a road over lands without lawful authority;153 for the trustees of a mutual benefit association to illegally vote themselves back pay, and to issue unauthorized certificates of membership.154

Of course a corporation's violation of a statute or resolution of the legislature which is unconstitutional, as a statute impairing the obligation of the contract between it and the state resulting from its charter, cannot be made a ground of forfeiture. 155 But where a corporation does business under a statute for a number of years, it is estopped to object that the legislature

51 La. Ann. 1827.

The illegal levy of assessments upon its stock by a corporation is no ground for proceedings by the state to dissolve it. People v. Rosenstein-Cohn Cigar Co. (Cal.) + 63

To justify proceedings by bank commissioners under a statute to dissolve a banking corporation on the ground that "it is so managing its concerns, that the public, or those having funds in its custody, are in danger of being defrauded thereby," it is not necessary that they shall be satisfied that there is a formed design on the part of the managers to cheat the bill holders or the depositors, but it is sufficient if they are satisfied that the condition of the bank, from its improper and illegal management, and the temptation to and danger

leans Debenture Redemption Co., of fraud growing out of it, are such that they ought to interfere to prevent it. Bank Commissioners v. Rhode Island Central Bank, 5 R. I. 12.

148 State v. Crawfordsville & Shannondale Turnpike Co., 102 Ind. 283; State v. Crawfordsville & Darlington Turnpike Co., 102 Ind.

149 State v. Urbana & Champaign Mutual Ins. Co., 14 Ohio, 7. 150 Com. v. Pittsburgh & Connellsville R. Co., 58 Pa. St. 26.

151 People v. Bogart, 45 Cal. 73. 152 North & South Rolling Stock Co. v. People, 147 Ill. 234.

153 State v. Kill Buck Turnpike Co., 38 Ind. 71.

154 State v. People's Mutual Benefit Ass'n, 42 Ohio St. 579.

155 Washington Bridge Co. v. State, 18 Conn. 53.

had no power to enact the statute, when proceedings are instituted against it by the state for violating the same. 156

(c) Nonuser of franchises, neglect of duty, etc.—It has been said that it is an implied condition of every corporate charter that the grantees shall act thereunder up to the expiration of the time for which they are incorporated, and if they fail to do so, the franchises granted may be withdrawn. And, as a general proposition, this is true. 157 It has been held, however, that the charter of a corporation should not be forfeited for nonuser unless it affects matters which are of the essence of the contract between it and the state, 158 nor for "acts of nonuser that do not amount to willful and repeated violations of the contract between the corporation and the state."159

The charter of a corporation may certainly be forfeited in proper proceeding for willful nonuser of its franchises, to the injury or prejudice of the public, for neglect to perform duties imposed upon it for the benefit of the public, or for rendering itself unable to perform such duties. 160 For example, it has been

Ins. Co., 60 How. Pr. (N. Y.) 82. 157 State v. New Orleans Gas Light & Banking Co., 2 Rob. (La.) 529. See, also, Darnell v. State, 48 Ark. 321; Chesapeake & Ohio Canal Co. v. Baltimore & Ohio R. Co., 4 Gill & J. (Md.) 1; Washington & Baltimore Turnpike Road v. State, 19 Md. 239; People v. Plainfield Avenue Gravel Road Co., 105 Mich. 9; State v. Minnesota Central Ry. Co., 36 Minn. 246; State v. Council Bluffs & Nebraska Ferry

Council Bluins & Nedraska Ferry Co., 11 Neb. 354; and other cases cited in the notes following. 158 Harris v. Mississippi Valley & Ship Island R. Co., 51 Miss. 602. And see State v. Farmers' College, 32 Ohio St. 487; State v. Council Bluffs & Nebraska Ferry Co., 11 Neb. 354

158 People v. Globe Mutual Life Turnpike Co. v. Maryland, 3 Wall. is. Co., 60 How. Pr. (N. Y.) 82. (U. S.) 210; Darnell v. State, 48 Ark. 321; People v. Pittsburg R. Co., 53 Cal. 694; Enfield Toll Bridge Co. v. Connecticut River Co., 7 Conn. 28; Ward v. Farwell, 97 Ill. 593; Illinois Health University v. People, 166 Ill. 171; Henderson Loan & Real Estate Ass'n v. People, 163 Ill. 196; State v. Pipher, 28 Kan. 127; State v. New Orleans Gas Light & Banking Co., 2 Rob. (La.) 529; Washington & Baltimore Turnpike Road v. State, 19 Md. 239; People v. Jack-son & Michigan Plank Road Co., 9 Mich 285; People v. Plymouth Plank Road Co., 32 Mich. 248; People v. Plainfield Avenue Grav-And see State v. Farmers' College, 22 Ohio St. 487; State v. Council Bluffs & Nebraska Ferry Co., 11
Neb. 354.
159 State v. Societe Republicaine, 9 Mo. App. 114. And see State v. Council Bluffs & Nebraska Ferry Co., 11 Neb. 354; State v. Pawtuxet Turnpike Corp., 8 R. I. 182.
160 Washington & Baltimore

People v. Plainfield Avenue Grav-People v. Plainfield Avenu held a cause of forfeiture for a corporation created for the purpose of furnishing a city and its inhabitants with water to willfully fail to do so for a long time, 161 for a corporation authorized and required to keep and maintain a ferry or bridge at a certain point to abandon its ferry, and fail to erect or maintain a bridge;162 for a railroad company to allow its road to be sold on execution: 163 for a railroad or turnpike company to make an unauthorized conveyance or long lease of its road, or a part thereof, to another company, and abandon its operation; 164 for a corporation to fail to keep its principal place of business, its books and records, and its principal officers within the state to such an extent as may be necessary for the jurisdiction and visitorial power of the state and its courts, and the efficient exercise thereof in all proper cases which concern the corporation.165

It has also been held a cause of forfeiture for a railroad company incorporated for the purpose of transporting both freight and passengers to refuse or fail to run passenger cars;166 for a railroad company to abandon a part of its route:167 or to

ple v. Hillsdale & Chatham Turn-452; State v. Rives, 5 Ired. (N. C.) 309; Attorney General v. Petersburg & Roanoke R. Co., 6 Ired. (N. C.) 456; Trustees of McIntire Poor School v. Zanesville Canal & Mfg. Co., 9 Ohio, 203, 34 Am. Dec. 436; State v. Pawtuxet Turnpike Corp., 8 R. I. 182, 521, 94 Am. Dec. 123; State v. Royalton & Woodstock Turnpike Co., 11 Vt. 431; State v. Pasumpsic Turnpike Co., 3 Vt. 178; State v. Milwaukee, Lake Shore & W. R. Co., 45 Wis. 579.

161 State v. Capital City Water Co., 102 Ala. 231. In this case it was held that in quo warranto to annul the charter of a water company because it had willfully failed for three years to furnish the city with a sufficient supply of water, an answer by the respondent that 53 Cal. 694. it had enlarged its works and in-

24 N. Y. 261, 82 Am. Dec. 295; Peo-creased its water supply up to a certain date, and was then negopike Road, 23 Wend. (N. Y.) 254; tiating for other wells, which People v. Fishkill & Beekman would supply all necessary de-Plank Road Co., 27 Barb. (N. Y.) mands, and that it ceased such negotiations because the city had declared its intention to exercise its option to purchase such water-works, was insufficient to constitute a defense.

> 162 State v. Council Bluffs & Nebraska Ferry Co., 11 Neb. 354.

> 163 State v. Rives, 5 Ired. (N. C.) 297, 309; State v. Minnesota Central Ry. Co., 36 Minn. 246.

164 State v. Atchison & Nebraska R. Co., 24 Neb. 143, 8 Am. St. Rep. 164; State v. Pawtuxet Turnpike Corp., 8 R. I. 182, 521, 94 Am. Dec.

165 State v. Milwaukee, Lake Shore & W. R. Co., 45 Wis. 579. And see infra, this section (k).

166 People v. Pittsburgh R. Co.,

167 People v. Albany & Vermont

fail to construct such a line as is required by its charter;168 or for a railroad or turnpike company to fail to comply with a provision in its charter requiring an annual statement of its income, disbursements, etc., to be made to the legislature or governor, for the purpose of enabling the legislature to regulate the tolls to be charged, or for other purposes;169 for a turnpike or plankroad company to neglect for a long time to properly construct or repair its road; 170 or for a bridge company to fail to rebuild its bridge within a reasonable time after its destruction by a flood, when the bridge is necessary to render a public road passable.171

It is a cause of forfeiture for a corporation organized for

R. Co., 24 N. Y. 261, 82 Am. Dec.

168 State v. Hazelton & Leetonia

Ry. Co., 40 Ohio St. 504. 169 Attorney General v. Petersburg & Roanoke R. Co., 6 Ired. (N. C.) 456; Com. v. Tenth Massachusetts Turnpike Corp., 11 Cush. (Mass.) 171. But see State v.

Road Co., 120 Ind. 337. 170 Washington Baltimore Turnpike Co. v. Maryland, 3 Wall. (U. S.) 210; Darnell v. State, 48 Ark. 321; Washington & Baltimore Turnpike Road v. State, 19 Md. 239; People v. Jackson & Michigan Plank Road Co., 9 Mich. 285; People v. Plymouth Plank Road Co., 32 Mich. 248; People v. Plainfield Avenue Gravel-Road Co., 105 Mich. 9; People v. Kingston & Middletown Turnpike Road Co., 23 Wend. (N. Y.) 193, 35 Am. Dec. 551; People v. Hillsdale & Chatham Turnpike Road, 23 Wend. (N. Y.) 254; People v. Fishkill & Beekman Plank Road Co., 27 Barb. (N. Y.) 445; State v. Royalton & Woodstock Turnpike Co., 11 Vt. 431; State v. Pasumpsic Turnpike Co., 3 Vt. 178; State v. Pawtuxet Turn-pike Corp., 8 R. I. 182, 521, 94 Am. Dec. 123. Unless some other penalty is prescribed by its charter. Habersham & Union Turnpike Co. v. Taylor, 73 Ga. 552. See infra, this section (o).

In a proceeding to forfeit the charter of a turnpike company on the ground of misuser in omitting to comply with the provisions of a general law to which it was subject in the original construction of its road, and also in failing to setts Turnpike Corp., 11 Cush. keep the road in repair, it was (Mass.) 171. But see State v. held necessary, in order to war-Brownstown & River Valley Gravel rant a judgment of forfeiture, not only that there should have been a deviation from the statute in the construction of the road, but also that the road should have been thereby rendered injurious to the public, and that the want of repairs should have been such as to render it dangerous or inconvenient to travelers. People v. Williamsburgh Turnpike Road Bridge Co., 47 N. Y. 586.

> Where a plank-road company had forfeited its franchises by permitting portions of its road to become impassable and dangerous, it was held that the fact that it afterwards surrendered these portions of its road, or subsequently made repairs, was no defense in proceedings to enforce the forfeiture. People v. Fishkill & Beekman Plank Road Co., 27 Barb. (N. Y.) 445.

> 171 People v. Hillsdale & Chatham Turnpike Road, 23 Wend. (N. Y.) 254; Enfield Toll Bridge Co. v. Connecticut River Co., 7 Conn. 28.

the promotion of education to transfer its property and remain inactive for nineteen years, though a suit was pending to recover some of the land formerly owned by it, but sold nineteen years before, 172 or for a manufacturing corporation to fail to comply with a provision of the manufacturing corporation law requiring it to make an annual statement of the amount paid on its capital stock.<sup>173</sup> Other cases are referred to in the note below.\*

In the case of a purely private corporation, failure of the corporators to organize under the charter is not such a nonuser as will warrant quo warranto proceedings to forfeit its char-And the charter of a purely private corporation will not be forfeited merely because it does not exercise all the powers conferred upon it, as where a manufacturing company does not manufacture all the articles which it is authorized to manufacture. 175

173 People v. Buffalo Stone & Cement Co., 131 N. Y. 140 (under a statute declaring that a corporation may be annulled whenever it shall offend against any provision of the act under which it was cre-

\* The charter of a bank may be forfeited for failure to make the report of its condition required by law for the protection of the public. State v. Seneca County Bank, 5 Ohio St. 171.

The charters of banks have been held liable to forfeiture because of suspension of specie payment, in violation of law, without any fault of the state. State v. Real Estate Bank, 5 Ark. 595, 41 Am. Dec. 109; Palfrey v. Paulding, 7 La. Ann. 363; State v. Commercial Bank of Cincinnati, 10 Ohio, 535; Commercial Bank of Natchez v. State, 6 Smedes & M. (Miss.) 599, 45 Am. Dec. 280; Planters' Bank v. State, 7 Smedes & M. (Miss.) 163; State v. Bank of South Carolina, 1 Speer (S. C.) 433; State v. New Orleans Gaslight & Banking Co., 2 Rob. (La.) 529. But failure to pay in specie is v. Burns, 114 N. C. 353.

172 State v. Pipher, 28 Kan. 127. ground of forfeiture only when it is required by law. State v. Tom-

beckbee Bank, 2 Stew. (Ala.) 30. In Reynolds v. State Bank, 18 Ind. 467, it was held that, since the act of congress making United States treasury notes a legal tender was within the constitution, state banks, by redeeming in treasury notes, did not expose their franchises to forfeiture under charter provisions that they should not at any time suspend or refuse payment in gold or silver of their obligations, etc.

Where a statute required the banks in a certain city to settle and pay in gold and silver the balances due each other upon a certain day of each week, it was held that it imposed no duty not previously imposed by law, and that, if a party in whose favor it was stipulated chose to waive the right, the state could not complain without showing some injury to the community. State v. New Orleans Gaslight & Banking Co., 2 Rob. (La.) 529.

174 State v. Simonton, 78 N. C.

175 Wadesboro Cotton Mills Co.

Where the legislature has, by express provision, fixed a period for which nonuser of its franchise by a corporation—as failure of a railroad company to operate its road—shall be cause for forfeiture of its franchise, nonuser for a less period is not ground of forfeiture, 176

- ---Inability of a corporation to perform public duties on account of its financial condition is no defense in proceedings by the state to forfeit its charter for failure to perform such duties. 177
- (d) Breach of conditions subsequent—(1) In general.—The charter of a corporation may also be forfeited in proper proceedings for a failure to comply with a condition subsequent prescribed therein, 178 as for failure of a railroad or turnpike company to commence or complete its road within a certain time, 179 for failure of a river improvement company to lock and slacken the river between certain points within the time limited in its charter, 180 for failure of a corporation authorized to improve a river or stream, and to collect tolls, to comply with its charter as to the condition in which the river or stream shall be kept, 181 for failure of a bridge company to commence construction of the bridge within a certain time, 182 for failure to comply with provisions as to subscription and payment of a certain amount of capital stock within a time prescribed, 183 or

179 Hughes v. Northern Pacific

183 People v. City Bank of Lead-

<sup>178</sup> State v. Nonconnah Turnpike Co., 1 Tenn. Cas. 511; People v. Co., 1 Tenn. Cas. 511; People v. County Elevated R. Co., 105 N. Y. City Bank of Leadville, 7 Colo. 27; Day v. Ogdensburgh & Lake 226; Com. v. Tenth Massachusetts Champlain R. Co., 107 N. Y. 129; Turnpike Corp., 11 Cush. (Mass.) State v. Nonconnah Turnpike Co., 171; State v. Council Bluffs & Ne- 1 Tenn. Cas. 511.

Henderson Loan & Real Estate Ass'n v. People, 163 Ill. 196; State v. Smith's Cas. 377..

v. Brownstown & River Valley Gravel Road Co., 120 Ind. 337; Ann. 678.

People v. Buffalo Stone & Cement Co., 131 N. Y. 140; and cases cited Bridge Co. v. Smith. 148 N. Y. 540. People v. Buffalo Stone & Cement Co., 131 N. Y. 140; and cases cited in notes following.

182 New York & Long Island Bridge Co. v. Smith, 148 N. Y. 540, in notes following.

<sup>176</sup> People v. Atlantic Avenue R. Ry. Co., 18 Fed. 106; People v. Co., 57 Hun (N. Y.) 378, 125 N. Y. Kingston & Middletown Turnpike Road Co., 23 Wend. (N. Y.) 193, 177 People v. Plainfield Avenue 35 Am. Dec. 551; People v. Water-Gravel-Road Co., 105 Mich. 9. ford & Stillwater Turnpike Co., 3 Am. Dec. (N. Y.) 580; In re King's County Elevated R. Co., 105 N. Y.

provisions requiring annual statements to the governor or legislature of receipts and disbursements. 184

As a general rule, even when the penalty of forfeiture and dissolution is not expressly imposed, all the duties or requirements enjoined by an act of incorporation or a general incorporation law are conditions attached to the grant or the franchise conferred, and must be substantially performed, or the corporation will subject itself to a forfeiture. 185 A requirement, however, may be so immaterial that it will not be considered that the legislature intended it as a condition subsequent, and, in such a case, failure to comply with the same will not be a ground of forfeiture. 186

In order to obtain a decree of forfeiture for breach of a condition subsequent prescribed in a charter, it need not be shown that the failure to comply with the condition was willful, and not the result of an honest mistake in the construction of the charter.187

—— (2) Substantial compliance with charter or statute sufficient.

-When proceedings are instituted against a corporation to forfeit its charter for misuser or neglect, on the ground that it has failed to comply with particular provisions of its charter, or of some other statute to which it is subject, it is sufficient, in order to defeat the proceedings, for it to show a substantial compliance with such provisions. For this reason it was held in a late Illinois case that a technical violation by a corporation of a statute requiring the directors to cause to be kept at its

tional Savings Bank, 129 Ill. 618; Co., 131 N. Y. 140.

184 Com. v. Tenth Massachusetts Turnpike Corp., 11 Cush. (Mass.) 171; Attorney General v. Petersburg & Roanoke R. Co., 6 Ired. (N. C.) 456.

Co., 1 Tenn. Cas. 511.

<sup>186</sup> See Harris v. Mississippi Valley & Ship Island R. Co., 51 Miss. 602, where the charter of a rail- supra,(b).(c).

ville, 7 Colo. 226; People v. Na- road company defined the termini of its road, and gave the general People v. Buffalo Stone & Cement direction, and required a survey of the route to be made, and a map made and filed in the office of the secretary of state within twelve months from the granting of the charter, and it was held that this was not a material condition of the charter, and that a failure to 185 State v. Nonconnah Turnpike comply therewith was no cause of forfeiture.

187 State v. Nonconnah Turnpike Co., 1 Tenn. Cas. 511. Compare principal office or place of business within the state correct books of account of all its business was not cause for forfeiting its franchises, where it substantially complied with the statute by keeping its books just across the state line from its Illinois office, and brought them to that office whenever demanded . by any stockholder or other person entitled to inspect them. 188

- -(3) Construction in case of doubt.—When there is any doubt as to the construction of a charter or statute prescribing conditions subsequent to be performed by a corporation, it should be so resolved as to avoid a forfeiture, if it can reasonably be done, for statutes are liberally construed to prevent forfeitures. 189
- (e) Inutility or impracticability of franchise or enterprise.— The charter of a corporation cannot be forfeited merely because its franchise or enterprise is useless or impracticable. 190 it has been held that the charter and franchises of a corporation organized for the purpose of reclaiming lands within a certain district of the state cannot be forfeited merely because the reclamation of the lands is impracticable;191 and that the charter of a corporation authorized to improve a river or stream, which is a public highway, cannot be forfeited merely because the improvements are not beneficial, where no such condition is prescribed in the charter. 192
- (f) Suspension or abandonment of business.—According to the cases referred to in a previous section, it is clear that willful abandonment of its business, or willful suspension without sufficient excuse, by a corporation which is charged with du-

189 State v. Brownstown & River Valley Gravel Road Co., 120 Ind.

<sup>192</sup> Appeal of Bennett's Branch Improvement Co., 65 Pa. St. 242.

<sup>188</sup> North & South Rolling Stock Co. v. People, 147 Ill. 234. See, also, Co. v. People, 147 III. 234. See, also, Valley Gravel Road Co., 120 Ind. People v. Kingston & Middletown Turnpike Road Co., 23 Wend. (N. Y.) 193, 35 Am. Dec. 551; People Connecticut River Co., 7 Conn. 28; v. Williamsburgh Turnpike Road & People v. Reclamation District No. & Bridge Co., 47 N. Y. 586; State v. Wood, 84 Mo. 378; Commercial Bank of Natchez v. State, 6 Pa. St. 242.

Smedes & M. (Miss.) 599; Chicago City R. Co. v. Story, 73 III. 541; State v. Farmers' College, 32 Ohio St. 487. St. 487.

ties for the benefit of the public, as in the case of railroad companies, turnpike companies, canal companies, ferry and bridge companies, and the like, so that the public welfare is affected, will generally be held sufficient ground for proceedings to forfeit its charter. 193 And even in the case of a corporation owing no peculiar duties to the public, an abandonment of its business with no intention to resume, or a long-continued suspension thereof, may be ground for forfeiture. 194

It has been held, however, that mere temporary suspension of business by a corporation—even a railroad company—is no ground for the forfeiture of its franchise, where there is no injury to the public, or where the suspension is because of a lack of patronage, and the corporation holds itself in readiness to resume business as soon as it can do so with profit,195 and that the charter of a purely private corporation will not be forfeited because of its failure to carry on all the business which it is authorized to carry on, as where a manufacturing company does not manufacture all the articles which it is authorized to manufacture.196

193 People v. Pittsburgh R. Co., State v. Cannon River Manufac-53 Cal. 694; State v. Rives, 5 Ired. turers' Ass'n, 67 Minn. 14; State v. (N. C.) 309; State v. Minnesota Commercial Bank of Manchester, Central Ry. Co., 36 Minn. 246; 13 Smedes & M. (Miss.) 569, 53 State v. Council Bluffs & Nebraska Am. Dec. 106; Henderson Loan & Ferry Co., 11 Neb. 354; State v. Real Estate Ass'n v. People, 163 Atchison & Nebraska R. Co., 24 Ill. 196; State v. Seneca County Neb. 143, 8 Am. St. Rep. 164; State v. Pawfuxet Turnnike Corp. 8 R. Neb. 143, 8 Am. St. Rep. 104; State v. Pawtuxet Turnpike Corp., 8 R. I. 182, 521, 94 Am. Dec. 123; People v. Albany & Vermont R. Co., 24 N. Y. 261, 82 Am. Dec. 295; People v. Plainfield Avenue Gravel-Road Co., 105 Mich. 9; State v. Pipher, 28 Kan. 127.

Where a corporation, authorized and required by its charter to keep and maintain a ferry or bridge R. 129, it was held that a mere across a river at a certain point, temporary suspension of its busioperated a ferry for a number of ness by a railroad company for a years, and then abandoned it, and failed to erect or maintain a and continued business without in-bridge, it was held that its fran-terruption, was not such nonuser chise should be forfeited. State as to operate as a forfeiture of v. Council Bluffs & Nebraska its charter. Ferry Co., 11 Neb. 354.

196 Wadesboro Cotton
194 State v. Pipher, 28 Kan. 127; v. Burns, 114 N. C. 353.

195 Com. v. Fitchburg R. Co., 12 Gray (Mass.) 180; Attorney General v. Bank of Niagara, Hopk. Ch. (N. Y.) 354; State v. Commer-Bank of Manchester, Smedes & M. (Miss.) 569, 53 Am. Dec. 106.

In Com. v. New York, Lake Erie & W. Coal & R. Co., 10 Pa. Co. Ct. year, where it afterwards resumed terruption, was not such nonuser

196 Wadesboro Cotton Mills Co.

-Statutory provision for forfeiture and dissolution.-By express statutory provision in some jurisdictions, abandonment of its business by a corporation, or suspension of business for a certain time, is made a cause of forfeiture or dissolution, and, under such a statute, abandonment or suspension of its business by a corporation for the time specified renders it subject to forfeiture of its charter and dissolution, in proceedings by the state or by a stockholder, according to the provisions of the statute, and this, without regard to the cause of the abandonment or suspension.197

In a New York case, where a corporation, organized for the business of marine insurance and the lending of money upon bottomry, by resolution of its stockholders resolved to suspend its business and appointed a committee to manage its estate and effects, and for more than a year afterwards failed to make contracts of insurance or to lend money on marine risks, and neglected to hold its annual meeting for the purpose of electing directors, it was held that it was subject to a statute providing that, whenever a corporation should suspend its ordinary and lawful business for a year, it should be deemed to have surrendered its rights, privileges, and franchises, and should be adjudged to be dissolved, and that a stockholder was entitled to an injunction restraining it and its officers from exercising any of its corporate rights, and to the appointment of a receiver to close up its affairs. And it was further held that it could not defeat a forfeiture by showing that it had, during the year, attended to the adjustment of losses upon risks previously

Ins. Co., 4 Sandf. Ch. (N. Y.) 559; Conro v. Gray, 4 How. Pr. (N. Y.) 166; Swords v. Northern Light Oil Co., 17 Abb. N. C. (N. Y.) 115; Kelsey v. Pfaudler Process Fermentation Co., 45 Hun (N. Y.) 10; barger Mill & Elevat People v. Atlantic Avenue R. Co., ling, 81 Ill. App. 30. 57 Hun (N. Y.) 378.

197 Hart v. Boston, Hartford & E. Under a statute authorizing a R. Co., 40 Conn. 524; People v. court of equity to appoint a receiv-Northern R. Co., 53 Barb. (N. Y.) er and dissolve a corporation where 98; Ward v. Sea Ins. Co., 7 Paige it ceases to do business, such au(N. Y.) 294; In re Jackson Marine thority attaches where the propthority attaches where the property of a corporation is seized under judgments amounting nearly to its assets, and is about to be sold, and it has no means with which to extricate itself. Shellabarger Mill & Elevator Co. v. Wilassumed, and to the business of collecting in and securing the corporate funds. 198

In another New York case it was held that a statute providing for the forfeiture of the charter of a corporation if it should suspend its ordinary and lawful business for more than a year did not admit of any excuse for such suspension. 199 Connecticut case, under a statute authorizing the court to render a decree dissolving a corporation whenever it should aban-

(N. Y.) 294. See, also, In re Jackson Marine Ins. Co., 4 Sandf. Ch. (N. Y.) 559.

statute that where an underground railway company had not, within the period prescribed by the statute, commenced the performance of its of its tunnel or railroad, nor begun legal proceedings to condemn its mandamus proceedings to compel might construct a tunnel and railway not authorized by its charter, was not a transaction of business, within the meaning of the People v. New York City Central Underground Ry. Co., 66 Hun (N. Y.) 633, 137 N. Y. 606.

In Swords v. Northern Light Oil Co., 17 Abb. N. C. (N. Y.) 115, it was held that a corporation might dissolved for suspension of business, where its property consisted of oil lands partly developed, that no oil had been taken for many years, that the supply of oil had gradually diminished, until the wells could no longer be operated at a profit, that the failure of the wells had crippled the company in its supply, and that the business of the company could not be continued without loss and damage.

In Kelsey v. Pfaudler Process Fermentation Co., 45 Hun (N. Y.) 10, the defendant corporation, organized for the manufacture, use,

198 Ward v. Sea Ins. Co., 7 Paige and sale of apparatus and process for making beer and other fermented liquors, became involved in litigation with a rival com-It was also held under such a pany claiming to own the same in-The vention. two companies agreed that the one which succeeded in the litigation should have three-fourths, and the other onebusiness, nor constructed any part fourth of the profits of the invention; that all the patents held by both companies should be assigned right of way, the commencement of to a new corporation, to be organized by the parties, each party the commissioner of public works reserving its rights under exist-to grant a permit to remove paveing licenses; that the new corpo-ments, in order that the company ration should have five directors, two of whom should represent the defeated party. The defendant succeeded in the litigation, the defeated new corporation was organized, the patents were assigned to it, its stock was divided between the two companies in the proportion agreed upon, the defendant's president was authorized to vote on its share of the new stock, and the new corporation thereafter represented the rights of both companies under the patents. The defendant kept up its own corporate organization, its officers continued to act as such, and it continued to issue licenses, collect royalties, and prosecute and defend actions in its own name, as before the arrangement. Under these circumstances it was held that it had not incurred a forfeiture of its franchise on the ground of suspension of its ordinary and lawful business.

190 People v. Northern R. Co., 53 Barb. (N. Y.) 98.

don its business and neglect for an unreasonable time to wind up its affairs, it was held that an application for such a decree could not be defeated by the fact that the abandonment of its business by the corporation was not of free choice, but compelled by legal proceedings and other causes which it could not resist.<sup>200</sup>

Where a statute provides for an action to dissolve a corporation if it shall suspend business for a specified time, such an action cannot be brought until after the lapse of the time specified. 201

(g) Inability to continue business .- It is no doubt safe to say that the charter of a corporation will be forfeited, and the corporation dissolved, if conditions arise which render it impossible for it to continue its business and perform the conditions upon which the charter was granted.202 But it has been held that the state is not entitled to a judgment forfeiting the charter of a corporation on the ground of inability to carry out a part of the design for which it was organized, where the fundamental design is being accomplished.203

The fact that a corporation's inability to continue business and performance of its duties to the public is due to its financial condition is no defense in proceedings to forfeit its charter for failure to perform such duties.204

201 In People v. Atlantic Avenue R. Co., 57 Hun (N. Y.) 378, 125 N. Y. 513, it was held that there was no conflict between section 1785 of the New York Code of Civil Procedure, providing that an action to dissolve a corporation may be maintained "where it has suspended its ordinary and lawful business for at least one year," and section 1798, providing that the attorney general may sue to vacate the charter of a corporation on the ground that it has "forfeited its privileges or franchises by a failure to exercise its powers," and that an action by the attorney general to dissolve a corporation on the ground of its suspension of business cannot be Gravel Road Co., 105 Mich. 9.

200 Hart v. Boston, Hartford & brought unless the suspension of E. R. Co., 40 Conn. 524. brought unless has continued for a year

202 See Chicago Life Ins. Co. v. Needles, 113 U. S. 574; State v. Real Estate Bank, 5 Ark. 595, 41 Am. Dec. 109; Carey v. Greene, 7 Ga. 79; Ward v. Farwell, 97 Ill. 593; Bank Commissioners v. Bank of Brest, Har. Ch. (Mich.) 106; State v. Commercial Bank of Manchester, 13 Smedes & M. (Miss.) 569, 53 Am. Dec. 106; People v. Bank of Niagara, 6 Cow. (N. Y.) Bank of Niagara, 6 Cow. (N. Y.)
196; People v. Bank of Hudson, 6
Cow. (N. Y.) 217; People v. Globe
Mutual Life Ins. Co., 60 How. Pr.
(N. Y.) 82; State v. Seneca County
Bank, 5 Ohio St. 176.

208 State v. Farmers' College, 32
Ohio St. 487.

(h) Insolvency and failure to pay debts—Assignment for benefit of creditors.—In the absence of a statutory provision on the subject, the mere insolvency of a corporation, or its refusal or failure to pay its debts on demand, does not authorize the forfeiture of its franchises and its dissolution, unless it appears that its insolvency is such that it cannot continue business and perform the conditions on which its charter was grant-Nor is an assignment by a corporation for the benefit of creditors sufficient ground for proceedings to forfeit its charter, where the corporation is not thereby rendered unable to perform the conditions upon which its charter was granted.206

It has been held, however, that if a corporation becomes insolvent, and the conditions are such that it is unable to continue the business for which it was created without injury to its creditors and stockholders, it becomes its duty to wind up its business, and that its charter may be forfeited in proceedings by the state if its fails to perform such duty.207

In some jurisdictions, statutes have been enacted making insolvency of a corporation, or insolvency for a certain length of time, a cause of forfeiture or dissolution in an action or proceeding by the state, or by a stockholder, or, in some states, by a creditor.208

Turnpike Co. v. Holthouse, 7 Ind.

That mere failure of a corporation to pay a debt is not such a nonfeasance as to authorize proceedings to forfeit its charter or dissolve it, see Aurora & Laughery Turnpike Co. v. Holthouse, 7 Ind.

205 People v. Bank of Washing-Real Estate Bank, 5 Ark. 595, 41 ton, 6 Cow. (N. Y.) 211; State v. Am. Dec. 109; Carey v. Greene, 7 Bailey, 16 Ind. 46; State v. Com-Ga. 79; Ward v. Farwell, 97 Ill. mercial Bank of Manchester, 13 593; Bank Commissioners v. Bank Smedes & M. (Miss.) 569, 53 Am. of Brest, Har. Ch. (Mich.) 106; Dec. 106; Aurora & Laughery chester, 13 Smedes & M. (Miss.) 569, 53 Am. Dec. 106; People v. Bank of Niagara, 6 Cow. (N. Y.) 196; People v. Bank of Hudson, 6 Cow. (N. Y.) 217; People v. Globe Mutual Life Ins. Co., 60 How. Pr. (N. Y.) 82; State v. Seneca County Bank, 5 Ohio St. 176.

59.
208 See People v. Bank of Pon206 State v. Commercial Bank of tiac, 12 Mich. 526; St. Louis & Manchester, 13 Smedes & M. Sandoval Coal & Mining Co. v. (Miss.) 569, 53 Am. Dec. 106; State v. Bailey, 16 Ind. 46, 79 Am. Dec. III. 170; Chicago Mutual Life Indemnity Ass'n v. Hunt, 127 Ill. 257; 207 Chicago Life Ins. Co. v. Kittredge v. Kellogg Bridge Co., 8
 Needles, 113 U. S. 574; State v. Abb. N. Cas. (N Y.) 168; Denike

(i) Alienation of property.—Though, as we have seen in a previous section, the alienation of all its property by a corporation, rendering it unable to continue its business, does not ipso facto operate to dissolve the corporation, 209 it has been held to be ground for proceedings to forfeit its charter.<sup>210</sup> And this is true, even though its charter may have empowered it to sell land and other property granted to it at the time of its organization.211

-Lease of property.-Whether or not a lease of its property by a corporation is ground for forfeiting its charter must depend upon the circumstances. Certainly, if the nature of the corporation and the term of the lease are such that the interests of the public are injuriously affected, as in the case of an ultra vires lease by a railroad company for a term of years, the charter of the corporation may be forfeited in proceedings by And the charter of a corporation may undoubtedly be forfeited if it makes an ultra vires lease of all its property for a long period, and thereby renders itself unable to carry on the business for which it was created. 213

The mere fact, however, that a lease of its property by a corporation was ultra vires is no ground for forfeiture or dissolution. In a Massachusetts case it was held that a statute authorizing dissolution of a corporation for "reasonable cause" imported more than a mere vague apprehension of some future mischief, and that there was no ground for decree of dissolution where one telegraph company had made a fraudulent lease of its line to another, but, after the filing of a petition for dissolu-

v. New York & Rosendale Lime & signments for the benefit of credicement Co., 80 N. Y. 599; Swords tors.
v. Northern Light Oil Co., 17 Abb.
N. Cas. (N. Y.) 115; People v. Excelsior Gaslight Co., 8 N. Y. Civ.

211 State v. Pawtuxet Turnpike Co., 8 R. I. 521, 94 Am. Dec. 123. Proc. Rep. 390.

<sup>209</sup> Ante, § 310.

<sup>&</sup>lt;sup>210</sup> State v. Pawtuxet Turnpike Co., 8 R. I. 521, 94 Am. Dec. 123; Smith v. St. Louis Mutual Life Ins. Co., 2 Tenn. Ch. 727; State v. Seneca County Bank, 5 Ohio St. 171. See, however, supra (h), as to as-

a turnpike company, empowered by its charter to sell land and other property granted to it at the time of its organization, sold its road.

<sup>&</sup>lt;sup>212</sup> Supra, this section (c).<sup>213</sup> State v. Atchison & Nebraska R. Co., 24 Neb. 143, 8 Am. St. Rep. 164; supra, this section, (c).

tion, the lease was cancelled by a vote of the directors of both companies.214 And in a New York case, where a manufacturing corporation temporarily leased its property to a person, who was to continue and carry on its business, it was held that the fact that the lease was unlawful was no ground for a suit by a portion of the stockholders to dissolve the corporation.<sup>215</sup>

In a late Iowa case, where a corporation organized under the laws of Iowa to build and maintain a bridge over the Missouri river between Iowa and Nebraska, and which had been granted the right to lay railroad tracks on the streets of a city in Iowa, leased its interests to a corporation of the same name, organized under the laws of Nebraska, the companies being owned and controlled by the same men, the Iowa court held that the lease was no ground for forfeiting the charter of the Iowa corporation.216

- (j) Failure to hold meetings.—Mere failure of a corporation to hold the meetings prescribed by its charter or articles, though its neglect may have continued for a considerable period, is not of itself ground for a forfeiture of its charter.217
- (k) Failure to keep or bring offices, officers, agencies, records, etc., within the state.—Failure of a corporation to comply with the law with respect to keeping its office or principal place of business, or its officers, or records, etc., within the state, may be made the ground of proceedings to forfeit its charter. 218 Thus it has been held in a late North Carolina case that, since the statutes of that state plainly contemplate that corporations created by or under its laws shall keep their principal offices, and certainly some of their agencies, within the state, the fail-

<sup>215</sup> Denike v. New York & Rosendale Lime & Cement Co., 80 N. Y. 599.

<sup>216</sup> State v. Omaha & Council Bluffs Railway & Bridge Co., 91 Iowa, 517.

<sup>&</sup>lt;sup>217</sup> State v. Barron, 58 N. H. 370; Mo. App. 114. See, also, Parsons notes following.

<sup>214</sup> In re Franklin Tel. Co., 119 v. Eureka Powder Works, 48 N. H. 66; Smith v. Natchez Steamboat

Co., 1 How. (Miss.) 479.
It does not ipso facto dissolve the corporation. See ante, § 309. 218 State v. Park & Nelson Lumber Co., 58 Minn. 330; Simmons v. Norfolk & Baltimore Steamboat Co., 113 N. C. 147, 37 Am. St. Rep. 614; State v. Topeka Water Co., 59 State v. Societe Republicaine, 9 Kan. 151; and other cases in the

ure of a domestic corporation to maintain its principal office within the state, as required by its articles of incorporation, and the withdrawal of all agencies from the state, is an abuse and misuser of its franchise, within the meaning of a statute authorizing a stockholder to institute proceedings for the dissolution of a corporation "for any abuse of its powers, to the injury of plaintiff or of the corporation."219 And in a Wisconsin case, the charter of a Wisconsin railroad corporation was forfeited in proceedings by the state, where it appeared that its principal offices were in New York city, that its books and records had always been kept in that city, that none of its principal officers resided in Wisconsin, and that, by reason of these facts, it had been impossible to enforce an attachment against the shares of stockholders of the company in actions in the Wisconsin courts.220

In Texas it was held, under the statutes of that state, that failure of the president or vice president and a majority of the directors of a corporation to reside in the state; as required by statute, was a cause of forfeiture.<sup>221</sup> A resident corporation's charter may be forfeited for refusal to bring its books into the state.222

It has been held that a statute providing that the secretary and treasurer of every domestic corporation shall reside, have their place of business, and keep the books of the corporation within the state, is not complied with by the residence within the state of a person who is nominally secretary and treasurer of a corporation, where the corporate business is all transacted in another state, and all its property situated there; and the

But where a corporation organized under the laws of Illinois kept ple, 147 Ill, 234. all its property in that state, and established an office there at which all corporate meetings were held, but had another office in Missouri, where much of its business was 40 N. J. Eq. 392, 396.

219 Simmons v. Norfolk & Balti- transacted, and where all its dimore Steamboat Co., 113 N. C. 147, rectors, officers, and stockholders 37 Am. St. Rep. 614. lived, it was held that it was not <sup>220</sup> State v. Milwaukee, Lake subject to forfeiture as being in Shore & W. Ry. Co., 45 Wis. 579. reality a foreign institution. North & South Rolling Stock Co. v. Peo-

> 221 State v. Southern Pacific R. Co., 24 Tex. 80, 121.

222 Huylar v. Cragin Cattle Co.,

charter of a corporation so conducting its business is subject to forfeiture.223

- (1) Mere wrongful intent.—Mere wrongful intent on the part of the officers and stockholders of a corporation to do acts which will constitute a violation of its charter at some future time, or to neglect at some future time to perform the duties imposed by its charter, or to fail to perform prescribed conditions subsequent, is no cause for forfeiture of its charter.<sup>224</sup> Thus, the charter of a railroad company cannot be forfeited because it intends at some future time to discontinue the operation of its road or a part thereof, or to otherwise neglect the performance of its full duty to the public, 225 or because it intends to violate its charter by connecting its road or consolidating with another company.226
- (m) Defective organization of corporations.—If there has been a failure to comply with conditions precedent in the organization of a corporation, so that there is merely a corporation de facto, as distinguished from a corporation de jure, as explained in a former chapter, quo warranto by the state will lie to forfeit its charter, and oust it from the exercise of corporate powers.<sup>227</sup> As we have seen, the question whether the corporation has been legally organized, and its right to exercise corporate powers, cannot be raised collaterally either by private individuals, by other corporations, or by the state.228

223 State v. Park & Nelson Lum- equity by a process of injunction, ber Co., 58 Minn. 330.

224 Com. v. Pittsburg & Connellsville R. Co., 58 Pa. St. 26; State v. Martin, 51 Kan. 462; Attorney General v. Superior & St. Croix R. Co., 93 Wis. 604; State v. Kingan, 51 Ind. 142; State v. Beck, 81 Ind. 500. And see Clancey v. Onon-daga Fine Salt Mfg. Co., 62 Barb. (N. Y.) 395.

"No mere intention or purpose in a corporation to violate its duty can constitute a case of forfeiture. \* \* \* The design clearly evinced to do an unlawful act may justify People v. La Rue, 67 Cal. 530; the interposition of a court of ante, § 80 et seq.

but it would be unjust, before the act was consummated to visit the corporate body itself with the extreme penalty of civil death and confiscation." Com. v. Pittsburg & Connellsville R. Co., 58 Pa. St.

<sup>225</sup> State v. Martin, 51 Kan. 462. 226 Com. v. Pittsburg & Connellsville R. Co., 58 Pa. St. 26.

227 Holman v. State, 105 Ind. 569; ante, § 93 et seq.

228 North v. State, 107 Ind. 356;

- (n) Subsequent compliance with the law.—Where a corporation forfeits its charter by misuser of its franchise, or by failure to perform the duties enjoined upon it as conditions of its creation and continuance, mere subsequent good behavior in such respects will not be a defense in proceedings by the state to enforce a forfeiture. Such is the dictum in a New York case, in which it was held that where a plank-road company had forfeited its franchise by permitting portions of its road to become impassable and dangerous, and proceedings were instituted by the state to enforce a forfeiture, it was no defense for the company to show that, after it had incurred the forfeiture, it surrendered those portions of its road, or made repairs.<sup>229</sup>
- (o) Particular penalty prescribed by charter or statute.—If the charter of a corporation or the general law under which it was organized imposes upon it a particular penalty, other than that of forfeiture, for doing an act prohibited, or not doing an act enjoined, it is to be presumed, unless there is something to rebut the presumption, that the legislature did not intend any other penalty, and the commission or omission of the act will not be cause for forfeiting the charter of the corporation.230 Thus it has been held that where the charter of a bank provides that, if it shall suspend specie payment, persons having the right to demand payment shall be entitled to recover damages, such suspension is not ground for forfeiture of its char-And where the charter of a turnpike company provides that, on its failure to keep its turnpike in repair, the toll gates shall be thrown open until repairs shall be made, its failure to keep its turnpike in repair, as required by its charter, is no ground for a forfeiture, the penalty of opening the gates being exclusive.232

Where a statute declares that it shall be a misdemeanor for

sham & Union Turnpike Co. v. 232 Habersham & Union Turn-Taylor, 73 Ga. 552; State v. pike Co. v. Taylor, 73 Ga. 552.

<sup>229</sup> People v. Fishkill & Beek-Brownstown & River Valley Gravel man Plank Road Co., 27 Barb. (N. Road Co., 120 Ind. 337; and cases in the notes following.

<sup>230</sup> State v. Real Estate Bank, 5 Ark. 595, 41 Am. Dec. 109; Haber- Ark. 595, 41 Am. Dec. 109.

any officer or agent of any street railway company to exact from any of its employes more than ten hours' labor per day, the charter of a company cannot be forfeited for its violation.<sup>233</sup> And where a statute requires a corporation to keep in its office an alphabetical list of its stockholders, showing their residence, number of shares, and amount of stock paid in, and prescribes a pecuniary penalty for its neglect to do so, and also requires it to publish a report of the amount of its capital stock, the amount thereof paid in, and the amount of its debts, and makes the trustees individually liable for its debts in case of its failure to do so, the corporation's failure to comply with either of these requirements is no ground for forfeiture of its charter.234

In New York, however, where a statute declares that a corporation may be annulled whenever it offends against any provision of the act under which it was created, it was held that failure of a manufacturing corporation to make an annual report of the amount paid upon its capital stock, as required by the statute under which it was created, was ground for its dissolution, although the only penalty prescribed in such statute was that, in case of its violation, all the trustees of the corporation should be liable for the corporate debts.235

(p) Fine or judgment of ouster.—Sometimes a statute authorizes the court, in its discretion, to impose a fine upon a corporation for violation of its charter or failure to perform prescribed conditions. Under such a statute, it has been held that, while a fine might be imposed for omission of some duty of minor importance, a judgment of forfeiture should be rendered for the nonperformance of a thing which is of the essence of the contract between the corporation and the state,—of "the very thing the performance of which was the purpose and object for which the company was instituted."236

 <sup>233</sup> People v. Atlantic Avenue R.
 235 People v. Buffalo S
 Co., 57 Hun (N. Y.) 378, 125 N. Y. ment Co., 131 N. Y. 140.

III. 79.

<sup>235</sup> People v. Buffalo Stone & Ce-

<sup>236</sup> People v. Kankakee River Im-234 Baker v. Backus' Adm'r, 32 provement Co., 103 III. 491, 1
 1. 79. Smith's Cas. 377.

(q) Acts and neglects of officers as acts and neglects of corporation.—When proceedings are instituted by the state to forfeit the charter of a corporation for ultra vires acts or improper neglect, the acts and neglects of its directors, trustees, or other managing officers, as such, though willful, are imputable to the corporation. "In its relations to the government, and when the acts and neglects of a corporation, in violation of its charter or the general law, become the subject of public inquiry with a view to a forfeiture of its charter, the willful acts and neglects of its officers are regarded as the acts and neglects of the corporation, and render the corporation liable to a judgment or decree of dissolution."237

A different rule, however, applies to acts of subordinate officers or agents not authorized or directed by the stockholders or directors. The charter of a corporation will not be forfeited for the acts of the managing agent in violation of his instructions, and without the consent or knowledge of the corpora-The charter of a bank will not be forfeited because of a violation of its charter by the cashier, where he acted contrary to the instructions and without the consent or knowledge of the directors.239

(r) Acts of stockholders as acts of corporation.—As we have seen in a former chapter, a corporation and its stockholders are separate and distinct persons in the law for the purpose of making contracts, taking, holding, and conveying property, and suing and being sued. For these purposes, the acts of the stockholders are not the acts of the corporation. This, however, is a mere fiction of the law, and when it is urged to an intent and purpose not within its reason, the courts will disregard it, even at law, and, looking behind the legal entity, will recognize the

239 State v. Commercial Bank of

<sup>237</sup> Angell & Ames, Corp. § 310. stitute of New York City, 7 Lans. See, also, Bank Commissioners v. (N. Y.) 304. Compare Belmont v. Bank of Buffalo, 6 Paige (N. Y.) Erie Ry. Co., 52 Barb. (N. Y.) 637. 497; Ward v. Sea Ins. Co., 7 Paige

238 Tuscaloosa Scientific & Art
(N. Y.) 297; Bank of Vincennes v. Ass'n v. State, 58 Ala. 54. State, 1 Blackf. (Ind.) 267, 12 Am. Dec. 234; People v. Dispensary & Manchester, 6 Smedes & M. (Miss.) Hospital Society of Women's In- 218, 45 Am. Dec. 280.

fact that the corporation is a collection of individuals. It has been held, therefore, that, where all the stockholders of a corporation, by transferring their shares to a committee or trustee, bring the corporation into an ultra vires and illegal trust or combination with other corporations, such acts of the stockholders will be regarded as the act of the corporation, when the trust or combination is made the basis of proceedings to forfeit its charter.240

## § 315. Waiver of forfeiture and estoppel of the state.

(a) In general.—It is well settled that when a corporation, by nonuser or misuser of its franchises, has rendered its charter and franchises liable to forfeiture in a proper proceeding by the state, the cause of forfeiture may be waived by the state. same is true where a corporation has rendered its charter liable to forfeiture by failure to comply with conditions subsequent prescribed in its charter, even when failure to comply therewith is expressly declared by the charter to be a cause of forfeiture and dissolution. And after such a waiver, neither the state nor individuals can set up or enforce a forfeiture.241

240 People v. North River Sugar shire Turnpike, 15 N. H. 162, 41 Refining Co., 121 N. Y. 582, 18 Am. Am. Dec. 690, 1 Smith's Cas. 370, St. Rep. 843, 2 Smith's Cas. 943, 1 Cum. Cas. 593; People v. Phoenix Cum. Cas. 570. See, also, State v. Bank, 24 Wend. (N. Y.) 431, 35 Standard Oil Co., 49 Ohio St. 137, Am. Dec. 634, 1 Smith's Cas. 373, 34 Am. St. Rep. 541; People v. 1 Cum. Cas. 597. Chicago Gas Trust Co., 130 Ill. 268, 17 Am. St. Rep. 319; Distilling & Cu. 29 Neb. State v. Real Estate Ill. 448, 47 Am. St. Rep. 200; State Bank, 5 Ark. 595, 41 Am. Dec. 109; N. Nebraska Distilling Co. 29 Neb. State v. Missisting Co. 20 State v. Missisting Co. 20 Neb. State v. Real Estate Neb. State v. v. Nebraska Distilling Co., 29 Neb. 700. And see ante, § 7(d).

In a late Pennsylvania case, however, it was held that the charter of a water company could not be forfeited, in proceedings by the state, because of the fact that inity of its stock to another corpora-

Fed. 498; State v. Real Estate Bank, 5 Ark. 595, 41 Am. Dec. 109; State v. Mississippi, Ouachita & Red River R. Co., 20 Ark. 495; Central & Georgetown Road Co. v. People, 5 Colo. 39; Enfield Toll Bridge Co. v. Connecticut River Co., 7 Conn. 28; Kellogg v. Union Co., 12 Conn. 7; People v. Missisdividual stockholders sold a major-sippi & Atlantic R. Co., 14 Ill. 440; People v. North Chicago Ry. Co., tion, and the latter undertook to 88 III. 537; People v. Ottawa Hyexercise control over its property draulic Co., 115 III. 281; Hatcher by mortgaging it. Com. v. Punx- v. Toledo, Wabash & W. R. Co., 62 sutawney Water Co. (Pa.) 47 Atl. Ill. 477; State v. Trustees of Vin-3. cennes University, 5 Ind. 77; State 241 State v. Fourth New Hamp- v. Bailey, 19 Ind. 452; Regents of

- (b) In case of dissolution, ipso facto, on failure to comply with conditions.—The doctrine of waiver by the legislature, by subsequent legislative acts, of a forfeiture of its charter by a corporation by failure to comply with a condition subsequent prescribed in the charter, does not apply where, by the terms of the charter, as explained in a former section,242 the corporation is ipso facto dissolved, and its franchises absolutely terminated by such failure. In such a case, the corporation, when it fails to perform the condition, ceases to exist, and the doctrine of waiver of forfeiture cannot apply.243
- (c) Implied waiver.—Waiver of a forfeiture by the legislature need not necessarily be expressly declared in a statute, but it may be implied. As a general rule, a waiver will be implied from acts of the legislature recognizing the subsequent and continued existence of the corporation as legal.<sup>244</sup>

v. Twenty Third Street R. Co., 54
How. Pr. (N. Y.) 168; Com. v. four years after an amendment of
Pittsburg & Connellsville R. Co., its charter, as the amendment is
58 Pa. St. 26; Hinchman v. Philadelphia & West Chester Turnpike
Road, 160 Pa. St. 150; State v.

244 State v. Fourth New HampPark of Charleston 2 McMull (S. Bank of Charleston, 2 McMull. (S. C.) 439, 39 Am. Dec. 135; La Grange & Memphis R. Co. v. Rainey, 7 Cold. (Tenn.) 420; Attorney General v. Superior & St. Croix R. Co., 93 Wis. 604; State v. Janesville Water Co., 92 Wis. 496; and cases cited in the notes following.

242 Ante, § 306.

243 State v. Fourth New Hampshire Turnpike, 15 N. H. 162, 41 Am. Dec. 690, 1 Smith's Cas. 370, 1 Cum. Cas. 593; State v. Old Town Bridge Corp., 85 Me. 17; People v. Manhattan Co., 9 Wend. (N. Y.) 351.

University of Maryland v. Williams, 9 Gill & J. (Md.) 365, 31 Lime Rock R. Co., 83 Me. 440, Am. Dec. 72; Planters' Bank v. wherein it was held that the four Bank of Alexandria, 10 Gill & J. years, at the end of which, under (Md.) 346; Richards v. Merrimack the Maine statute, a charter of ince Connecticut River Railroad, 44 corporation becomes forfeited for N. H. 127; People v. Manhattan failure of the corporation to or-Co., 9 Wend. (N. Y.) 351; In reganize and commence business New York Elevated R. Co., 70 N. within that time, do not run Y. 337; Central Crosstown R. Co. against a corporation organizing v. Twenty Third Street R. Co. 54 and commencing business within

shire Turnpike, 15 N. H. 162, 41 Am. Dec. 690, 1 Smith's Cas. 370, 1 Cum. Cas. 593. See, also, State v. Real Estate Bank, 5 Ark. 595, 41 Am. Dec. 109; State v. Mississippi. Ouachita & Red River R. Co., 20 Ark. 495; People v. Mississippi & Atlantic R. Co., 14 Ill. 440; People v. Ottawa Hydraulic Co., 115 Ill. 281; State v. Trustees of Vin-University, 5 Ind. cennes Farnsworth v. Lime Rock R. Co., 83 Me. 440; Richards v. Merrimack & Connecticut River Railroad, 44 N. H. 127; People v. Manhattan Co., 9 Wend. (N. Y.) 351; In re New York Elevated R. Co., 70 N. a waiver of a cause of forfeiture may be implied from an act of the legislature ratifying acts done by the corporation after the cause of forfeiture arose, as a transfer of property or privileges,245 or from an act granting additional powers, or extending the time for performing conditions subsequent,246 or an act filling the offices of certain directors which have become vacant, and have not been filled because of the suspension of the corporation's business.247 Borrowing of money by the state from a bank, under an act of the legislature, after it has committed acts in violation of its charter, or has been guilty

Mull. (S. C.) 439, 39 Am. Dec. other cases cited in notes 241 et 135; La Grange & Memphis R. Co. seq., supra.

v. Rainey, 7 Cold. (Tenn.) 420; Where the legislature enacted a Baltimore & Ohio R. Co. v. Marshstatute amending the charter of a all County Sup'rs, 3 W. Va. 319; railroad company, expressly recognized to the control of the control

Croix R. Co., 93 Wis. 604.

ings in quo warranto by the state privileges, and which had been conferred upon it. and vesting the same in the assignee. The decision was put up- ing or reviving the charter of a on the ground that no object was corporation operates as a waiver of to be gained by a forfeiture either the right to enforce a forfeiture for in reference to the public or to private individuals, but it might well have been based upon the ground that there had been a waiver. State v. Centreville Bridge Co., 18 Ala. 678. See, also, People v. Ottawa Hydraulic Co., 115 III. 281.

246 State v. Fourth New Hampshire Turnpike, 15 N. H. 162, 41 turnpike company to complete its Am. Dec. 690, 1 Smith's Cas. 370, road was not a waiver of a pre-Bridge Co. v. Connecticut River failure to comply with conditions, Co., 7 Conn. 28; People v. Misbut the decision cannot be sussissippi & Atlantic R. Co., 14 Ill. tained. Judge Cowen dissented. 440; People v. Ottawa Hydraulic <sup>247</sup> State v. Trustees of Co., 115 Ill. 281; Farnsworth v. cennes University, 5 Ind. 77.

Y. 337; Com. v. Pittsburg & Con- Lime Rock R. Co., 83 Me. 440; nellsville R. Co., 58 Pa. St. 26; La Grange & Memphis R. Co. v. State v. Bank of Charleston, 2 Mc-Rainey, 7 Cold. (Tenn.) 420; and

Attorney General v. Superior & St. nizing its continued existence as a corporation, and affirming its right 245 In an Alabama case, proceed- to exercise the power of eminent domain in the manner prescribed to forfeit the charter of a corpora- by the general law in addition to tion were dismissed where it ap- the method pointed out in its charpeared that after the alleged cause ter, it was held that the right of of forfeiture arose the legislature the state to enforce a forfeiture of had passed an act ratifying an as- its charter theretofore incurred by signment by the corporation of the nonuser was thereby waived. Atpowers torney General v. Superior & St. upon it, Croix R. Co., 93 Wis. 604.

An act of the legislature extendnonperformance of conditions subsequent prescribed by the charter. In re Mechanics' Society, 31 La.

Ann. 627.

In People v. Kingston & Middletown Turnpike Road Co., 23 Wend. (N. Y.) 193, 35 Am. Dec. 551, it was held that an act of the legislature extending the time for a Cum. Cas. 593; Enfield Toll vious forfeiture of its charter by

247 State v. Trustees of Vin-

of neglect of duty, is a waiver of the right to forfeit its charter for such causes.248

In a leading New Hampshire case, the charter of a turnpike company required it to lay before the legislature, at the end of every six years after the setting up of any toll gate, an account of its expenditures and profits, and provided in effect that, if it should fail to do so, it should forfeit its charter. The company failed to furnish accounts for about thirty years after toll gates were established by it, but it then began to furnish them regularly every six years, and they were accepted by the legislature as sufficient and satisfactory. After the first account was furnished, the legislature also passed an act authorizing the company to change the route of its road in certain towns, and it accepted the act and made the change at great expense. Under these circumstances, it was held that the right to enforce a forfeiture of the charter for the failure to furnish accounts during the first thirty years was waived.<sup>249</sup> In another New Hampshire case it was held that the right of the state to enforce a forfeiture of the charter of a corporation, because it had mortgaged its property in violation of its charter, was waived by the passage of an act by the legislature authorizing a foreclosure of the mortgage.250

Of course the acts relied upon as constituting an implied waiver by the legislature of a forfeiture of its charter by a corporation must be such as to show an intention to waive the forfeiture. If they are consistent with an intention to afterwards insist upon the forfeiture, there is no waiver.<sup>251</sup>

<sup>1</sup> Cum. Cas. 593.

<sup>248</sup> State v. Real Estate Bank, 5 Middletown Turnpike Road Co., 23 Ark. 595, 41 Am. Dec. 109.

Wend. (N. Y.) 193, 35 Am. Dec.

Wend. (N. Y.) 193, 35 Am. Dec.

249 State v. Fourth New Hamp
521; State v. Equitable Loan & Investment Ass'n of Sedalia, 142

Am. Dec. 690, 1 Smith's Cas. 370, Mo. 325.

Usurpation by a corporation of 250 Richards v. Merrimack & authority to acquire and hold land Connecticut River Railroad, 44 N. for purposes not within the objects of its creation is not waived by the 251 People v. Phoenix Bank, 24 appointment by the legislature of a Wend. (N. Y.) 431, 35 Am. Dec. committee to investigate its prop-634, 1 Smith's Cas. 373, 1 Cum. erty, and ascertain if it is properly Cas. 597; People v. Kingston & taxed, and a report by the commit-

an intention is clearly shown by acts of the legislature, as in the cases referred to above, conferring additional powers upon the corporation, or otherwise authorizing it to do acts which it could not or would not do except on the assumption of a continuance of its existence without being liable to forfeiture for past acts or neglect.<sup>252</sup> But where a corporation had forfeited its corporate privileges by taking usury, it was held that the forfeiture was not waived by the subsequent appointment of a state director by the governor and senate, even assuming that they had the power to waive a forfeiture, 253 since, until the forfeiture was enforced in proper judicial proceedings by the state, it was the duty of the governor and senate, as well as all others, to treat the corporation as a legally existing body; and the appointment, therefore, was not inconsistent with an intention on the part of the state to afterwards enforce the forfeiture.254

In a late Missouri case it was held that a statute which operated merely prospectively did not operate as a waiver of prior acts of misuser. 255

(d) Mere acquiescence and lapse of time.—Mere acquiescence by the public in the violation of its charter by a corporation, or mere lapse of time before commencement of proceedings to enforce a forfeiture, where there has been no express waiver, and no recognition of the continued existence of the corporation as legal, will not generally operate as a waiver of the

er, see infra, this section, (g).

tee in the affirmative, for this is 239, it was held that the state not a concession by the state that might enforce a forfeiture of the the corporation has authority to charter of a turnpike company for hold the property. People v. Pull-nan's Palace-Car Co., 175 Ill. 125.

252 See notes 245-250, supra.

253 That they have no such power, see infra. this section, (g). the strength of which it contract-254 People v. Phoenix Bank, 24 ed a loan secured by tolls, and ap-Wend. (N. Y.) 431, 35 Am. Dec. plied all the tolls to the repair of 634, 1 Smith's Cas. 373, 1 Cum. the road.

Las. 597.

In Washington & Baltimore Investment Ass'n of Sedalia, 142
Turnpike Road v. State, 19 Md. Mo. 325.

cause of forfeiture, so as to bar a proceeding by the state.256 But it has been held that long delay in instituting such proceedings will be held a waiver of causes of forfciture, where such causes are known, and the corporation is allowed to continue operations and incur expenses in the belief that there has been a waiver.257

- (e) Continuing cause of forfeiture.—A waiver by an act of the legislature of the right of the state to forfeit the charter of a corporation for misuser, nonuser, or breach of condition subsequent, only operates as to causes of forfeiture existing at the time of the passage of the act. And therefore, where a cause of forfeiture continues after the passage of an act of the legislature constituting a waiver (as in the case of failure to comply with a continuing condition subsequent), the act does not operate as a waiver of the right to enforce a forfeiture for the cause arising after its passage.258
- (f) Knowledge of cause of forfeiture.—In order that acts of the legislature in relation to a corporation may be deemed a waiver of the right of the state to enforce a forfeiture of its. charter for misuser or nonuser of its franchises, the acts must have been passed by the legislature with knowledge of the existence of the cause of forfeiture.<sup>259</sup> Such knowledge, however, need not necessarily be expressly proved. It may undoubtedly be presumed, in the absence of evidence to the con-

pike Co., 10 Conn. 157.

In a late Illinois case, in which quo warranto proceedings were brought against the Pullman's Palace-Car Company to forfeit its charter for various usurpations, it was held that the company could not successfully set up as a defense that the usurpations com-plained of had continued for a number of years with the knowl- Turnpike Corp., 11 Cush. (Mass.) edge of the state, and that the state 171; State v. Real Estate Bank, 5 had waived and acquiesced therein, since the right of the state to v. Manhattan Co., 9 Wend. (N. Y.) complain of usurpations by a cor-

<sup>256</sup> State v. Pawtuxet Turnpike poration, and to enforce a for-Co., 8 R. I. 521, 94 Am. Dec. 123; feiture of its charter therefor, could State v. Norwalk & Danbury Turn- not be defeated by the imputation of laches. People v. Pullman's Palace-Car Co., 175 Ill. 125.

> 257 State v. Janesville Water Co., 92 Wis. 496; State v. Bailey, 19 lnd. 452. And see the dictum in Kellogg v. Union Co., 12 Conn. 7.

> 258 State v. Nonconnah pike Co., 1 Tenn. Cas. 511.

> 259 Com. v. Tenth Massachusetts

trary, from the fact that the misuser or nonuser was generally known in the community.260

- (g) Who may waive a forfeiture—(1) In general.—As a general rule, no one can waive a forfeiture of its charter by a corporation except the state.<sup>261</sup> Furthermore, waiver of a forfeiture of its charter and franchises by a corporation, like the creation of a corporation, is a legislative act, and is not within the power of any executive or judicial officer of the state, nor within the power of any body of men other than the legislature. A forfeiture, therefore, cannot be waived by the governor and the senate alone, for the act of the senate alone is not the act of the legislature.<sup>262</sup> Nor can a cause of forfeiture be waived by the attorney general, 263 or by a court or judge. 264
- -(2) Waiver by municipality.—Where, however, conditions subsequent, express or implied, are required to be performed by a corporation solely for the benefit of a municipal corporation, its acts may be relied upon as a waiver of the right to enforce a forfeiture for failure to perform the condi-In a late Wisconsin case, on an application of the attorney general for leave to bring proceedings in quo warranto to forfeit the charter and franchises of a city water company for failure to keep an account of the cost of the construction of its plant, so as to enable the city to exercise an option to purchase the plant, as was required by the ordinance granting the company its franchise, it was held that the acts of the city should be considered in determining whether the right to enforce a forfeiture had been waived. And, as it appeared that the city, with full knowledge of the grounds relied upon for forfeiture, had for a considerable time compelled the company to improve its plant at great expense, that its present stock-

note 241 et seq.

Vend. (N. Y.) 431, 35 Am. Dec.

2º1 People v. Phoenix Bank, 24 Cas. 597.

Wend. (N. Y.) 431, 35 Am. Dec.

2º3 See New Orleans & Carroll634, 1 Smith's Cas. 373, 1 Cum. ton R. Co. v. City of New Orleans,
Cas. 597; Chicago City Ry. Co. v. 34 La. Ann. 429. People, 73 Ill. 541.

<sup>262</sup> People v. Phoenix Bank, 24 Co., 38 Barb. (N. Y.) 323.

 <sup>260</sup> See the cases cited supra, because 241 et seq.
 Wend. (N. Y.) 431, 35 Am. Decapte 241 et seq.

 634, 1 Smith's Cas. 373, 1 Cum.

<sup>264</sup> See People v. Rensselaer Ins.

holders and officers had attempted in good faith to show the cost of the plant, and that the alleged failure to keep a proper account occurred before the present stockholders became interested in the company, the court, in the exercise of its discretion, denied the application on the ground that the right to enforce a forfeiture had been waived.265

- (h) Conditional waiver.—Waiver of a forfeiture of its charter by a corporation may be conditional, instead of absolute. In such a case, the state may still enforce the forfeiture if the conditions are not performed or fulfilled.266 Thus, where the legislature, after failure of a railroad company to complete its road within the time fixed by its charter, passed an act extending the time, provided the road should not be sold to a certain party, and the road was afterwards sold to such party, it was held that the forfeiture for the original default was not waived.267
- (i) Violation of contract by the state.—When proceedings are instituted by the state to determine and enforce a forfeiture of the charter of a corporation for misuser or nonuser, or for failure to perform conditions subsequent, the state is not precluded from enforcing the forfeiture by the fact that it has itself violated the contract between it and the corporation. Thus, in scire facias against a turnpike company to forfeit its charter for nonperformance of its duties under the same, it was held that it was no defense for it to show that exclusive franchises had been granted to it by the state, and that the state, in violation of the grant, had created another corporation, to the injury of the defendant, and to the profit of the state 268

## PROCEDURE AND JURISDICTION.

§ 316. In general.—At common law, a proceeding to forfeit the charter of a corporation is either by scire facias, or by an

<sup>92</sup> Wis. 496.

<sup>265</sup> State v. Janesville Water Co., Farnsworth v. Minnesota & Pacific R. Co., 92 U. S. 49.
267 La Grange & Memphis R. Co.
Rainey, 7 Cold. (Tenn.) 420;
268 Washington & Baltimore v. Rainey, 7 Cold. (Tenn.) 420;

information in the nature of quo warranto, instituted and prosecuted by the attorney or solicitor general on behalf of the state. In most jurisdictions, however, the mode of procedure is now prescribed by statute.

As a general rule, in the absence of a statute, a court of equity has no jurisdiction to decree a forfeiture of the charter of a corporation, or otherwise dissolve it, either in a suit by the attorney or solicitor general on behalf of the state, or in a suit by the corporation itself, or by stockholders or creditors. In some states, however, such jurisdiction has been conferred by statute.

Neither a court nor the legislature of one state or country has jurisdiction to dissolve a corporation created by another state or country.

# § 317. Mode of procedure at common law.

At common law, the mode of proceeding against a corporation to enforce a forfeiture of its charter, or to oust it from the unauthorized exercise of corporate powers, was by scire facias, or by an information by the attorney or solicitor general in the nature of the writ of quo warranto. Formerly scire facias was the proper remedy where there was a legal existing body capable of acting, but which had been guilty of an abuse of its powers and franchises, and it is still so in some jurisdictions,269 while quo warranto was the proper remedy where a body undertook to act as a corporation without legal authority. In the latter case, scire facias would not lie.

In this country, an information in the nature of quo warranto, brought by the solicitor or attorney general in the name and on behalf of the state, is now the proper remedy in most jurisdictions in all cases, except where some statutory remedy has been substituted, whether there is a legal corporation which

Turnpike Co. v. Maryland, 3 Wall. Road v. State, 19 Md. 239; Wash-(U. S.) 210. And see Washington ington & Baltimore Turnpike Co. & Baltimore Turnpike Road v. v. Maryland, 3 Wall. (U. S.) 210. State, 19 Md. 239.

A scire facias proceeding by the

State, 19 Md. 239.

A scire facias proceeding by the 269 Rex v. Pasmore, 3 Term R. state to forfeit the charter of a 199; Slee v. Bloom, 5 Johns. Ch. corporation is a civil action. (N. Y.) 366, 1 Cum. Cas. 113, 116; Washington & Baltimore Turnpike Washington & Baltimore Turnpike Road v. State, 19 Md. 239.

has forfeited its right to continue, or merely a de facto corporation exercising corporate powers without authority.<sup>270</sup> information in the nature of quo warranto by the attorney general in behalf of the state to forfeit the charter of a corporation for misuser or nonuser, or for failure to perform a condition subsequent which is expressly declared a cause of forfeiture, is a remedy at common law, and it may be brought whenever a cause of forfeiture arises. It is not necessary that there shall be any general or special statute authorizing it to be brought.271

Pendency of proceedings under a statute by the directors of an insolvent corporation to dissolve it and distribute its assets through a receiver does not bar an action by the attorney general to enforce a forfeiture of its charter, for the statute is merely permissive, and does not exclude the common-law remedy. Both actions may be carried on at the same time, but a judgment of dissolution in one action will operate as an abatement of the other.272

<sup>270</sup> People v, Kankakee River Where a railroad company has Improvement Co., 103 Ill. 491, 1 ceased to do business, and has no Smith's Cas. 377; Wheeler v. Pull- office or agency in any county in man Iron & Steel Co., 143 Ill. 197, 1 Smith's Cas. 379; State v. Fourth chises having been surrendered un-New Hampshire Turnpike, 15 N. H. 162, 41 Am. Dec. 690, 1 Smith's Cas. 370, 1 Cum. Cas. 593; People tinues in the county in which it v. Phoenix Bank, 24 Wend. (N. Y.) 431, 35 Am. Dec. 634, 1 Smith's Cas. 373, 1 Cum. Cas. 597; State v. Cas. 373, 1 Cum. Cas. 597; State v. White's Creek Turnpike Co., 3 the annual meetings of its stockwhite's Creek Turnpike Co., 3 the annual meetings of its stockwhite's Creek Turnpike Co., 3 the annual meetings of its stockwhite's Creek Turnpike Co., 3 the annual meetings of its stockwhite's Creek Turnpike Co., 3 the annual meetings of its stockwhite's Creek Turnpike Co., 3 the annual meetings of its stockwhite's Coentry County, and therefore proceedings by the state to forfeit its charter county, and therefore proceedings by the state to forfeit its charter county, and therefore proceedings by the state to forfeit its charter county, and therefore proceedings by the state to forfeit its charter county, and therefore proceedings by the state to forfeit its charter county, and therefore proceedings by the state to forfeit its charter county, and therefore proceedings by the state to forfeit its charter county, and therefore proceedings by the state to forfeit its charter county, under a statute providing that an action shall be commenced in the county in which the defendant resides. Eel River R. Co. v. State, 155 Ind. 433.

State V. Southern Pacific R.

Co., 24 Tex. 80; State v. Equitable Loan & Investment Ass'n of Sedalia, 142 Mo. 325, and numerous lia, 142 Mo. 325, and numerous other cases cited in connection with this subject.

the state, all its property and frander a lease in perpetuity to another company, its legal residence conhad its principal office at the time it ceased to do business, although the annual meetings of its stock-

272 People v. Murray Hill Bank, 10 App. Div. (N. Y.) 328.

#### § 318. By what authority proceedings must be instituted.

In England, a proceeding to determine and enforce a forfeiture of the charter of a corporation was in the name and by the authority of the king. In this country, unless there is statutory provision to the contrary, such a proceeding is instituted by, and can only be instituted by, authority of the state. It cannot be instituted and prosecuted by private individuals, nor even by the attorney or solicitor general, if he is acting solely on behalf of private individuals, and not ex officio on behalf and by authority of the state. "An information for the purpose of dissolving the corporation, or of seizing its franchises," said Chief Justice Parsons in a Massachusetts case, "cannot be prosecuted but by the authority of the commonwealth, to be exercised by the legislature, or by the attorney or solicitor general, acting under its direction, or ex officio in its behalf. For the commonwealth may waive any breaches of any condition expressed or implied, on which the corporation was created; and we cannot give judgment for the seizure by the commonwealth, of the franchises of any corporation, unless the commonwealth be a party in interest to the suit, and thus assenting to the judgment."273

The attorney general cannot be compelled by mandamus to

Ins. Co., 5 Mass. 230, 4 Am. Dec.

273 Com. v. Union Fire & Marine Co., 97 Mich. 147; Hovelman v. Kansas City Horse R. Co., 79 Mo. 50, 1 Smith's Cas. 369. See, also, 632; Sewall's Falls Bridge v. Fisk, Gaylord v. Fort Wayne, Muncie & 23 N. H. 171; State v. Paterson & C. R. Co., 6 Biss. 286, Fed. Cas. Hamburg Turnpike Co., 21 N. J. No. 5,284; Ross v. Chicago, Bur-Law, 9; Terhune v. Potts, 47 N. J. lington & Q. R. Co., 77 Ill. 127; Law, 218; Buncombe Turnpike Co. People v. North Chicago Ry. Co., v. McCarson, 1 Dev. & B. (N. C.) People v. North Chicago Ry. Co., 88 Ill. 537; Atchafalaya Bank v. Dawson, 13 La. 497; State v. Atchafalaya Bank v. Co., 8 Jones L. (N. C.) 476; Bass torney General, 30 La. Ann. 954; v. Roanoke Navigation & Water-In re Louisiana Savings Bank & Power Co., 111 N. C. 439; Com. v. Safe Deposit Co., 35 La. Ann. 196; Farmers' Bank, 2 Grant's Cas. Planters' Bank v. Bank of Alexandria, 10 Gill & J. (Md.) 346; Bank, 2 Ashm. (Pa.) 170; Appeal New Central Coal Co. v. George's of Western Pennsylvania R. Co., Creek Coal & Iron Co., 37 Md. 537; Hodges v. Baltimore Union Passenger Ry. Co., 58 Md. 603; Rice v. pike Road, 160 Pa. St. 150; La National Bank of Commonwealth, Grange & Memphis R. Co. v. 126 Mass. 300; Heap v. Heap Mfg. institute quo warranto or other proceedings to forfeit the charter of a corporation.274

It is competent for the legislature to confer upon private individuals authority to institute proceedings against a corporation to determine and declare a forfeiture of its charter, and it has done so in some jurisdictions.<sup>275</sup>

#### § 319. Jurisdiction of courts of equity.

It is well settled, as a general principle, that, unless jurisdiction is conferred by statute, courts of equity have no jurisdiction to decree a dissolution of a corporation, or declare a forfeiture of its charter for misuser or nonuser, but the only remedy is at law, as shown in the preceding sections. And this is true, whether the suit be brought by a stockholder or other private individual,276 or by the attorney or solicitor general in

v. White's Creek Turnpike Co., 3 v. White's Creek Turnpike Co., of Tenn. Ch. 163; State v. Butler, 15 Lea (Tenn.) 104; State v. Rio Grande R. Co., 41 Tex. 217; State v. Paris Ry. Co., 55 Tex. 76. 274 State v. Attorney General, 30 La. Ann. 954; State v. Paterson 2. Herburg Turnpike Co. 21 N

& Hamburg Turnpike Co., 21 N. J. Law, 9. Contra, State v. Berry, 3 Gil. (Minn.) 190.

<sup>275</sup> See State v. Consolidation Coal Co., 46 Md. 1; Tuscaloosa Scientific & Art Ass'n v. State, 58 Ala. 54; post, § 320.

276 Wheeler v. Pullman Iron & Steel Co., 143 Ill. 197, 1 Smith's Cas. 379; Hardon v. Newton, 14 Blatchf. 376, Fed. Cas. No. 6,054, 1 Cum. Cas. 487.

The following cases are to the same effect:

United States: Gaylord v. Ft. Wayne, Muncie & C. R. Co., 6 Biss. 286; Republican Mountain Silver Mines v. Brown, 19 U. S. App. 203, 58 Fed. 644.

California: Neall v. Hill, 16 Cal. 145, 76 Am. Dec. 508.

District of Columbia: Morrow v. Edwards, 20 D. C. 475.

Illinois: People v. Weigley, 155 Ill. 491; Coquard v. National Linseed Oil Co., 171 Ill. 480, affirming

67 Ill. App. 20; Hunt v. Le Grand Roller Skating Rink Co., 143 Ill.

Iowa: Wallace v. Pierce-Wallace Publishing Co., 101 Iowa, 313, 63

Am. St. Rep. 389. Kentucky: Chambers v. Baptist Education Society, 1 B. Mon. 215; Oldham v. Mt. Sterling Improvement Co., 45 S. W. 779.

Maryland: Mason v. Supreme Court of Equitable League of Baltimore, 77 Md, 483, 39 Am. St. Rep. 433: Barton v. International Fraternal Alliance of Baltimore, 85

Massachusetts: Folger v. Columbian Ins. Co., 99 Mass. 274, 96 Am. Dec. 747; Cheshire Iron Works v. Gay, 3 Gray (Mass.) 531. Mississippi: Bayless v. Orne, 1

Freem. Ch. 161.

New Jersey: Society for Establishing Useful Manufactures v. Morris Canal & Banking Co., 1 N.
J. Eq. 157, 21 Am. Dec. 41; Doremus
v. Dutch Reformed Church, 3 N.
J. Eq. 349; Jersey City Gaslight
Co. v. Consumers' Gas Co., 40 N. J. Eq. 427; Elizabethtown Gaslight Co. v. Green, 46 N. J. Eq. 118, 49 N. J. Eq. 329. New York: Attorney General v.

the name and on behalf of the state.<sup>277</sup> A court of equity, in the absence of statutory provision, cannot dissolve a corporation on the ground that the act of incorporation was fraudulently obtained from the legislature, 278 or on the ground that the organization of the corporation under a general law was fraudulent as against the state or as against individuals. remedy in such a case is by proceedings in quo warranto by the attorney general on behalf of the state.<sup>279</sup>

Where the members of an unincorporated association in the District of Columbia met and decided to incorporate under an act of congress, and a minority of the members withdrew, and filed a certificate of incorporation under the name of the unincorporated association, and obtained possession of its personal property, before the incorporation of the majority, it was held that a court of equity had no jurisdiction, at the suit of the majority of the members against the minority, to dissolve the corporation formed by the minority, on the ground that its

1 Edw. Ch. 84; Howe v. Deuel, 43 Barb. 504; Doyle v. Peerless Petroleum Co., 44 Barb. 239; Water-bury v. Merchants' Union Express Co., 50 Barb. 157; Belmont v. Erie Ry. Co., 52 Barb. 637; Attorney General v. Bank of Niagara, 1 Hopk. Ch. 354; Kincaid v. Dwi-nelle, 59 N. Y. 548; Denike v. New York & Rosendale Lime & Cement Co., 80 N. Y. 599.

Rhode Island: Hodges v. New England Screw Co., 3 R. I. 9; Paulino v. Portuguese Beneficial Ass'n, 18 R. I. 165.

Tennessee: State v. Merchants' Insurance & Trust Co., 8 Humph. 235; Parker v. Bethel Hotel Co., 96 Tenn. 252.

Vermont: Ottaquechee Woolen

Co. v. Newton, 57 Vt. 451.
Virginia: Pixley v. Roanoke
Navigation Co., 75 Va. 320.

West Virginia: Hurst v. Coe, 30 W. Va. 158; Law v. Rich (W. Va.) 35 S. E. 858.

Wisconsin: Strong v. McCagg,

Utica Ins. Co., 2 Johns. Ch. 371; 55 Wis. 624; Hinckley v. Pfister, Verplanck v. Mercantile Ins. Co.. 83 Wis. 64; Independent Order of Foresters of Canada v. United Order of Foresters, 94 Wis. 234.

277 Attorney General v. Tudor Ice Co., 104 Mass. 239, 6 Am. Rep. 227, 1 Smith's Cas. 381, 1 Cum. Cas. 585; Attorney General v. Stevens, 1 N. J. Eq. 369, 22 Am. Dec. 526; Attorney General v. Utica Ins. Co., 2 Johns. Ch. (N. Y.) 371; Attorney General v. Bank of Niagara, Hopk. Ch. (N. Y.) 354; People v. Equity Gas Light Co., 141 N. Y. 232; People v. Weigley 155 Ill. 491; State v. Merchants' Insurance & Trust Co., 8 Humph. (Tenn.) 235.

 $^{278}\, Clarke$  v. Brooklyn Bank, 1 Edw. Ch. (N. Y.) 361 (where it was claimed that a charter of a bank was fraudulently obtained by the distribution of shares to the members of the legislature).

279 Morrow v. Edwards, 20 D. C.
 475; Attorney General v. Stevens,
 1 N. J. Eq. 369, 22 Am. Dec. 526.

charter was obtained by fraud. The proper remedy, it was said, was through proceedings by the attorney general of the United States, in which the legality of the incorporation could be ascertained and determined.280

After a corporation has been dissolved, however, by a judgment of forfeiture at law, or otherwise, a court of equity has jurisdiction, unless deprived thereof by a statute prescribing a different remedy, to administer the assets of the corporation by means of a receiver, and to protect and enforce the rights of stockholders and creditors therein.281

And, according to a decision in a Michigan case, even before a corporation has been dissolved at law, there may be circumstances under which a court of equity, for want of any adequate remedy at law, will have the power, under its general jurisdiction in cases of a trust relation, and to afford relief against fraud, to grant relief to a stockholder of a corporation, even to the extent of dissolving the corporation and winding up its affairs. Thus, even in the absence of any statute, it was held in a late Michigan case that a court of equity had jurisdiction, at the suit of a stockholder, to appoint a receiver and wind up the affairs of a corporation, where a majority of the stockholders had for a long time fraudulently excluded the complaining stockholder from participation in the management and profits of the corporation, and managed it in their own interest and for their own profit only.

280 Morrow v. Edwards, 20 D. C. instance of creditors, to wind up the affairs of such a corporation, the statutory remedy being ex-Water Co., 115 Ala. 156; Western clusive. It was further held that North Carolina R. Co. v. Rollins, the statutory remedy must be pur-82 N. C. 523. See post, § 328(b). sued within the three years, and In North Carolina it has been that a failure to proceed within former equity jurisdiction for the of its insolvency. Von Glahn v. appointment of a receiver, at the De Rosset, 81 N. C. 468.

held that the statute of that state that time was a complete defense which continued the existence of as against creditors of the corpodefunct corporations for three ration, not only to the corporation years after the expiration of their itself, but also to stockholders charters, for the purpose of bring-who by the charter of the corpora-ing and defending suits and clostion were made individually reing up their business, ousted the sponsible for its debts in the event

"The general rule," said Judge McGrath, "undoubtedly is that courts of equity have no power to wind up a corporation. in the absence of statutory authority. This rule is, however, subject to qualifications. It has been held that, when it turns out that the purposes for which a corporation was formed cannot be attained, it is the duty of the company to wind up its affairs; that the ultimate object of every ordinary trading corporation is the pecuniary gain of its stockholders; that it is for this purpose, and no other, that the capital has been advanced; and if circumstances have rendered it impossible to continue to carry out the purpose for which it was formed with profit to its stockholders, it is the duty of its managing agents to wind up its affairs. To continue the business of the company under such circumstances would involve both an unauthorized exercise of the corporate franchises and a breach of the charter contract. 'When a number of stockholders combine to constitute themselves a majority in order to control the corporation as they see fit, they become, for all practical purposes, the corporation itself, and assume the trust relation occupied by the corporation towards its stockholders. Although stockholders are not partners, nor strictly tenants in common, they are the beneficial joint owners of the corporate property. having an interest and power of legal control in exact proportion to their respective amounts of stock. The corporation itself holds its property as a trust fund for the stockholders, who have a joint interest in all its property and effects, and the relation between it and its several members is, for all practical purposes, that of trustee and cestui que trust. several persons have a common interest in property, equity will not allow one to appropriate it exclusively to himself, or to impair its value to the others. Community of interest involves mutual obligation. Persons occupying this relation towards each other are under an obligation to make the property or fund productive of the most that can be obtained from it for all who are interested in it; and those who seek to make a profit out of it, at the expense of those whose rights in it are the same as their own, are unfaithful to the relation they have assumed, and are guilty, at least, of constructive fraud.' This corporation has utterly failed of its purpose, not because of matters beyond its control, but because of fraudulent mismanagement and misappropriation of its funds. Complainant has a right to insist that it shall not continue as a cloak for a fraud upon him, and shall not longer retain his capital to be used for the sole advantage of the owner of the majority of the stock, and a court of equity will not so far tolerate such a manifest violation of the rules of natural justice as to deny him the relief to which his situation entitles him. I think a court of equity, under the circumstances of this case, in the exercise of its general equity jurisdiction, has the power to grant to this complainant ample relief, even to the dissolution of the trust relations. \* A receiver will be appointed, and the affairs of this corporation wound up."282

Injunction.—As we have seen in another chapter, a court of equity has no jurisdiction of a bill or information by the attorney general in the name and on behalf of the state to restrain a corporation from engaging in transactions which are either not authorized or prohibited by its charter, where the acts sought to be enjoined do not constitute a public nuisance or threaten any peculiar injury to the public. The remedy is at law by an information in the nature of quo warranto.283 A court of

In a late federal case it was held shown that the affairs of the corthat, while the general rule is that a court of equity is without jurisdiction, in the absence of statutory authority, to decree the dissolution of a private corporation which is a solvent and going concern, and to that end sequestrate its property and appoint a receiver, yet such court may always grant courted by relief against such a cortex. equitable relief against such a corporation whenever a sufficient Ice Co., 104 Mass. 239, 6 Am. Rep. cause for such relief is shown, up- 227, 1 Smith's Cas. 381, 1 Cum. Cas. on the ordinary principles of equi- 585; Attorney General v. Utica

232 Miner v. Belle Isle Ice Co., ty jurisprudence. And it was held 93 Mich. 97, 2 Cum. Cas. 234. See, that such a case authorizing disso-also, O'Connor v. Knoxville Hotel Co., 93 Tenn. 708. receiver is made out where it is In a late federal case it was held shown that the affairs of the cor-

equity, however, has jurisdiction of a suit by a stockholder of a corporation to enjoin a corporation, its officers, and the other stockholders from fraudulent or ultra vires acts, where the circumstances are such as to render the exercise of such jurisdiction necessary for the protection and enforcement of his rights.<sup>284</sup> And a suit may be maintained under some circumstances to enjoin acts constituting a public nuisance.285

#### § 320. Statutory jurisdiction to dissolve corporations.

In most jurisdictions, if not in all, statutes have been enacted providing the method of forfeiting the charters of corporations for misuser or nonuser of their franchises, or for other specified causes, and giving jurisdiction of proceedings for this purpose to particular courts. Generally the statutory proceeding to forfeit the charter of a corporation is an information in the nature of quo warranto by the solicitor or attorney general in his official name, or in the name of the state or the people; but sometimes a different mode of procedure is provided.<sup>286</sup>

In some states, by statute, proceedings to forfeit the charter of a corporation may be brought in the name of the state on the relation of private individuals, or by a private individual in his own name.<sup>287</sup> Except as explained in the preceding section,

ante, § 208 et seq.

284 Ante, § 210.

285 Ante, § 209.

286 See Com. v. Slifer, 53 Pa. St. 71; People v. Stanford, 77 Cal. 360; People v. Dashaway Ass'n, 84 Cal. 114.

As to the venue of statutory proceedings, see State v. Mobile & Girard R. Co., 108 Ala. 29; Weigley v. People, 51 Ill. App. 51; Bel Air Social, Literary, Musical & Dramatic Club v. State, 74 Md. 297; Mahoney Mutual Assessment Life Ass'n v. Com., 14 Wkly. Notes Cas. (Pa.) 370.

As to the jurisdiction and procedure in New York under section 18, c. 689, of the banking corporations law of 1892, to dissolve a cor-

Ins. Co., 2 Johns. Ch. (N. Y.) 371; poration upon report of the superintendent of banking that it is conducting its business in an unsafe manner, or is insolvent, and that it is inexpedient for it to continue longer in business, see People v. Mercantile Co-Operative Bank, 53 App. Div. (N. Y.) 295; People v. Republic Savings & Loan Ass'n, 53 App. Div. (N. Y.) 384.

As to the jurisdiction and procedure in New York to forfeit the charter of a corporation or dissolve it when it has failed to organize or commence business within two years, or has suspended business for a year or more, see People v. Ramapo Water Co., 51 App. Div. (N. Y.) 145.

287 See Tuscaloosa Scientific & Art Ass'n v. State, 58 Ala. 54; Miller v. Town of Palermo, 12 Kan. 14.

a private individual, whether a creditor or a stockholder or a stranger, cannot institute and prosecute such proceedings unless the statute expressly allows him to do so, and then only when the circumstances and his relation to the corporation bring him within the statute.<sup>288</sup> Such statutes are constitutional.<sup>289</sup>

In some states, jurisdiction has been conferred by statute upon courts of equity, or other courts, where the distinction between courts of law and equity has been abolished, to decree a dissolution of a corporation and to wind up its affairs, in specified cases, at the suit of individual stockholders, or of creditors, and the jurisdiction of the courts under such statutes have been upheld.<sup>290</sup> Under such a statute, the court has no

288 See People v. Grand River of the attorney general, to oust a Bridge Co., 13 Colo. 11, 16 Am. St. corporation of its franchise beRep. 182; Coquard v. National Linseed Oil Co., 171 Ill. 480, affirming
67 Ill. App. 20; Hunt v. Le Grand
Roller Skating Rink Co., 143 Ill.
118; Miller v. Town of Palermo,
12 Kan. 44; State v. Attorney General, 30 La. Ann. 954; Com. v.
Philadelphia, Germantown & N.
Ry. Co., 20 Pa. St. 518; Hurst v.
Coe, 30 W. Va. 158.
Under an Alabama statute any

Under an Alabama statute any person, on giving security for costs, may bring an action to vacate the charter of a corporation (Code, § 3167), or to oust persons acting as a corporation without being duly incorporated (Code, § 3170). State v. Webb, 97 Ala. 111, 38 Am. St.

Rep. 151.

that a statute (Gen. St. c. 145, §§ 16, 22), providing that any person whose private rights or interests have been injured or endangered Heap v. Heap Mfg. Co., 97 Mich. through the exercise, by a private 147. corporation or by persons claim- <sup>289</sup> Hunt v. Le Grand Ring to be such, of any franchise Skating Rink Co., 143 Ill. 118. not conferred upon them, may file an information in the nature of Steel Co., 143 Ill. 197, 1 Smith's quo warranto to determine the Cas. 379; Ward v. Farwell, 97 Ill. right of such corporation or persons to exercise the franchise in nity Ass'n v. Hunt, 127 Ill. 257; question, did not authorize the Life Association of America v. filing of an information in the Fassett, 102 Ill. 315; Hunt v. Le nature of quo warranto by a pri- Grand Roller Skating Rink Co., 143 vate person, without the consent Ill. 118; Chicago Life Ins. Co. v.

have surrendered the rights, privileges, and franchises granted by any act of incorporation, or acquired under the laws of this state, and shall be adjudged to be dissolved, it was held that, if the statute authorizes a bill in chancery to dissolve a corporation for insolvency, it does not abrogate In Massachusetts it was held the common-law rule that the state must bring it through its attorney general, or authorize such bill to be exhibited by a stockholder.

289 Hunt v. Le Grand Roller

290 Wheeler v. Pullman Iron &

jurisdiction to dissolve a corporation unless the conditions specified in the statute have arisen.<sup>291</sup> A statute providing for the dissolution of a corporation after judgment and execution against it, or on its insolvency, by an action on the application of the attorney general in a certain court, gives the court no authority to dissolve a corporation, at the suit of an individual, because of a violation of its charter.<sup>292</sup> And a statute providing that a court shall have jurisdiction of actions against domestic corporations on any cause of action arising within the state does not give it jurisdiction of a suit to dissolve a corporation and to appoint a receiver of its property.293

In some states, statutes have also been enacted providing for judicial proceedings for the voluntary dissolution of corporations under certain circumstances. Such proceedings can be maintained only when the circumstances specified in the statute exist, and, to sustain a decree of dissolution in such proceedings, the facts essential to the exercise of jurisdiction must appear upon the record of the court.294 And the provisions of

Mining Co. v. Sandoval Coal & Mining Co., 116 Ill. 170; Wolf v. Underwood, 91 Ala. 523; Hurst v. Coe, 30 W. Va. 158.

376, Fed. Cas. No. 6,054, 1 Cum. 376, Fed. Cas. No. 6,054, 1 Cum. Cas. 487; Wheeler v. Pullman Iron & Steel Co., 143 Ill. 197, 1 Smith's Cas. 379; People v. Weigley, 155 Ill. 491; Coquard v. National Linseed Oil Co., 171 Ill. 480, affirming 67 Ill. App. 20; Hurst v. Coe, 30 W. Va. 158; State v. Merchants' Insurance & Trust Co., 8 Humph (Tenn.) 225; In re Rease. 8 Humph. (Tenn.) 235; In re Pensacola Lumber Co., 8 Ben. 171, Fed. Cas. No. 10,959; Law v. Rich (W. Va.) 35 S. E. 858.

Thus where a statute empowers a court of equity to dissolve a corporation and wind up its affairs (1) on the application of any shareholder, if the corporation has voted to wind up its affairs, or has abandoned its business, and thereabandoned its business, and there-after neglected, within a reason- 8 Ben. 171, Fed. Cas. No. 10,959.

Auditor of Public Accounts, 101 Ill. able time, or in a proper manner, 82; St. Louis & Sandoval Coal & to wind up its affairs and distribute its assets among its stockholders; or (2) upon the petition of onethird of the stockholders,-such a court cannot dissolve a corpora-291 Hardon v. Newton, 14 Blatchf. tion on an application of a shareholder owning less than one-third of the stock, where the corporation has not voted to wind up its affairs, nor abandoned its business. though the other stockholders and the officers may be conducting its business improperly and dishonestly. Hardon v. Newton, 14 Biatchf. 376, Fed. Cas. No. 6,054, 1 Cum. Cas. 487.

See, also, as to suits by stockholders, post, chapter xxii. And as to suits by creditors, see

post, chapter xxv.

<sup>292</sup> Folger v. Columbian Ins. Co., 99 Mass. 267, 96 Am. Dec. 747. <sup>293</sup> Brahe v. Pythagoras Association, 4 Duer (N. Y.) 658, 11 How. Pr. 44.

the statute as to the mode of procedure must be complied Notice of the application for dissolution, or service of the petition, or an order to show cause, etc., when required by the statute, is necessary to give the court jurisdiction.296

Pendency of bankruptcy proceedings.—On an application for a decree to wind up a corporation under a state statute authorizing a court of equity, on application of any stockholder, to render a decree dissolving any corporation, and winding up its affairs, whenever it has abandoned the business for which it was organized, and has neglected for an unreasonable time to wind up its affairs and distribute its effects among its stockholders, such a decree may be rendered notwithstanding the fact that the corporation has been proceeded against under the federal bankruptcy law, and its property is in the hands of assignees in bankruptcy.297

## § 321. Jurisdiction of legislature or courts over foreign corporations.

The legislature of one state or country may, subject to some qualifications, regulate corporations created by another state or country, and doing business within its limits. And the courts of a state or country have jurisdiction to interfere under some circumstances with the acts of a foreign corporation owning property and doing business within the limits of such state or country, in order to prevent an abuse of trust by the corporation, or otherwise protect or enforce private rights. But nei-

See In re Mart, 22 Abb. N. Cas. N. Y. 261; In re French Mfg. Co., (N. Y.) 227; In re Marietta Build- 12 Hun (N. Y.) 488. ing & Loan Ass'n, 10 Lanc. Bar And see ante, § 308. (Pa.) 37.

295 In re Pyrolusite Manganese Co., 29 Hun (N. Y.) 429; Láke Ontario Nat. Bank v. Onondaga County Bank, 7 Hun (N. Y.) 549; In re French Mfg. Co., 12 Hun (N. Y.) 488; In re Marietta Building & Loan Ass'n, 10 Lanc. Bar (Pa.) 37.

As to the powers of the court in such proceedings, see In re Binghamton General Electric Co., 143 E. R. Co., 40 Conn. 524.

<sup>296</sup> Freeman's Nat. Bank v. Smith, 13 Blatchf. 220, Fed. Cas. No. 5,089; Farmers' Bank of Delaware v. Beaston, 7 Gill & J. (Md.) 421; People v. Seneca Lake Grape & Wine Co., 52 Hun (N. Y.) 174; In re Christian Jensen Co., 128 N.

297 Hart v. Boston, Hartford &

ther the legislature nor the courts of a state or country have the power to declare a forfeiture of the charter of a foreign corporation, or to otherwise dissolve such a corporation. can be done only by the legislature or the courts of the state or country by which the corporation was created.<sup>298</sup> The courts of a state, however, may inquire into the question whether a foreign corporation has forfeited its right to exist by acts or neglect which, of their own force, work a dissolution.299

The jurisdiction of the legislature or courts of a state to forfeit the charter of a corporation created by or under laws of that state is in no way affected by the fact that the corporators have also received charters from other states.300

## IV. EFFECT OF DISSOLUTION.

- § 322. In general.—When a corporation has been legally dissolved, it ceases to exist, and it follows that
- (1) It cannot afterwards exercise any of the franchises or powers conferred upon it by its charter, or otherwise act as a corporate body.
- (2) At common law, debts due to or by the corporation are extinguished, but this rule has very generally been changed by statute. And even in the absence of a statute, a court of equity will collect debts due to a corporation for the benefit of creditors and stockholders, and will satisfy debts due by the corporation out of its assets.
  - (3) At common law, all the real estate of a dissolved corporation reverts to the grantors or their heirs, and all its personal estate vests in the king or state, and this is still true as to some kinds of corporations. The rule, however, has been very generally changed by statute, and even in the absence of a statute, a court of equity, in the case of modern business corporations, will apply

298 Society for Propagation of Barb. (N. Y.) 140; Merrick v. Van the Gospel v. Town of New Haven, Santvoord, 34 N. Y. 208; Howell v. 6 Wheat. (U. S.) 464; Republican Chicago & N. W. Ry. Co., 51 Barb. Mountain Silver Mines v. Brown, (N. Y.) 378. And see post, chap-19 U. S. App. 203, 58 Fed. 644; ter xxvi.

Carey v. Cincinnati & Chicago R.
Co., 5 Iowa, 357; Importing & Experting Co. of Georgia v. Locke 50 porting Co. of Georgia v. Locke, 50 300 Hart v. Boston, Hartford & Ala. 332; Murray v. Vanderbilt, 39 E. R. Co., 40 Conn. 524.

their assets to the payment of their debts, and distribute what remains among their stockholders.

- (4) At common law, a cause of action in favor of or against a corporation for a tort does not survive its dissolution, but the rule has been changed to some extent by statute.
- (5) At common law, no action can be brought by or against a corporation after its dissolution, and actions pending at the time of its dissolution abate. This rule also has been changed to some extent by statute.
- (6) The transferability of its shares of stock ceases on the dissolution of a corporation.

When a corporation is dissolved by an absolute repeal of its charter under a reservation of the power to repeal the same, by expiration of the time limited in its charter, by a surrender of its charter accepted or authorized by the legislature, by a valid judgment forfeiting its charter, or in any other legal mode, as explained in the preceding sections, it no longer exists for any purpose, unless there is some statutory provision continuing its existence, and therefore, as will be shown more specifically in the following sections, it no longer has any capacity or power either to enter into contracts, or to take, hold, or convey property, or to sue or be sued, or to exercise any other franchise or power conferred upon it by its charter. Like a dead natural person, it has ceased to have any existence. 301

# Dissolution may be set up collaterally.

It necessarily follows from this that the dissolution of a corporation from any cause may be shown in any case in which

R. Co., 105 U. S. 13, 2 Smith's Cas. 791; Miami Exporting Co. v. Gano, 720, 1 Cum. Cas. 538; Thornton v. 13 Ohio, 269; White v. Campbell, Marginal Freight Ry. Co., 123 5 Humph. (Tenn.) 38; and other Cass. 32, 1 Cum. Cas. 462; People v. O'Brien, 45 Hun (N. Y.) 519, 111 the notes following.

N. Y. 1, 7 Am. St. Rep. 684, 2 Smith's Cas. 728; Bradley v. Reppell, 133 Mo. 545, 54 Am. St. Rep. from the opinion of Mr. Justice 685; Saltmarsh v. Planters' & Miller, in Greenwood v. Union Merchants' Bank of Mobile, 17 Freight R. Co., 105 U. S. 13, 2 Ala. 761; Bank of Mississippi v. Smith's Cas. 720, 1 Cum. Cas. 538.

the existence of the corporation is properly in issue, collaterally as well as in a direct proceeding by an information in the nature of quo warranto, and by private individuals as well as by the state. 302

This does not conflict at all with the rule referred to in a former section, that the forfeiture of its charter by a corporation for misuser or nonuser, or for failure to perform conditions subsequent, cannot be set up collaterally, for, until the forfeiture is judicially determined and decreed in a direct proceeding, there is no dissolution, but merely a cause of forfeiture, if the state sees fit to enforce it. 303 After the forfeiture has been judicially determined and decreed in proper proceedings, there is then a dissolution, which may be shown collaterally.

The fact that a corporation has been dissolved by the death of its members may be shown in a collateral proceeding, and by private individuals as well as by the state.<sup>304</sup> And though there are a few decisions to the contrary, 305 the same is true, by the great weight of authority, when a corporation is dissolved by the expiration of its charter.<sup>306</sup> When a corporation has absolutely ceased to exist, equity may, in a proper case, enjoin threatened acts of a person assuming to act for it.307

## § 324. When dissolution takes effect.

When proceedings are instituted against a corporation to forfeit its charter and dissolve it, either by the attorney general on behalf of the state, or by a stockholder under a statute, there

302 Blackwell v. State, 36 Ark. 178; Carey v. Cincinnati & Chicago R. Co., 5 Iowa, 357; Dobson v. Simonton, 86 N. C. 492; Chesapeake & Ohio Canal Co. v. Baltimore & Ohio R. Co., 4 Gill & J. (Md.) 1; Attorney General v. Chicago & Evanston R. Co., 112 Ill. 520; and other cases more specif- Paola Town Co., 20 Kan. 397; ically cited in the notes preceding Dobson v. Simonton, 86 N. C. 492; and following.

308 Ante, § 313.

304 Blackwell v. State, 36 Ark. 178.

305 Miller v. Newburg Orrel Coal Co., 31 W. Va. 836, 13 Am. St. Rep. 903; Bushnell v. Consolidated Ice Machine Co., 138 Ill. 67.

 306 Bradley v. Reppell, 133 Mo.
 545, 54 Am. St. Rep. 685; Krutz v. ante, § 305.

807 Attorney General v. Chicago & Evanston R. Co., 112 Ill. 520.

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is no dissolution until judgment of forfeiture. And if a judgment of forfeiture is rendered, but an appeal is taken or writ of error sued out by the corporation, there is no dissolution before affirmance of the judgment. It has therefore been held that, although a corporation cannot, after its dissolution, enter into a contract or be sued, nor a judgment be rendered against it,308 a bond executed by a corporation on appeal from a judgment forfeiting its charter is valid, although the judgment is affirmed; 309 and that a judgment rendered against a corporation pending an appeal from a judgment forfeiting its charter is valid, although the judgment of forfeiture is affirmed.310

#### § 325. Effect of dissolution with respect to franchises.

The dissolution of a corporation not only terminates its franchise to be a corporation, but, as stated in a former section, it also prevents it from further exercising any other franchise which has been conferred upon it by the legislature.311 example, a corporation authorized by its charter to operate a railroad cannot operate the same after its charter has expired, or been repealed, or forfeited in judicial proceedings by the A banking corporation, after expiration or annulment of its charter, cannot discount or purchase a bill of exchange as a business transaction, 313 or make new loans or issue new notes designed to circulate as money.314 And a corporation owning a mill privilege, on which it has erected and maintained a dam, cannot exercise its franchises after a judgment of ouster in quo warranto proceedings.315

<sup>312</sup> People v. O'Brien, 45 Hun (N. 174.

<sup>315</sup> Campbell v. Talbot, 132 Mass.

In a Kansas case, where a bridge company had constructed a bridge over a river under a charter authorizing it to take tolls. and the bridge was used as a thoroughfare uninterruptedly and without molestation, except that tolls were collected, the corporation having no property in the approaches to the bridge, or in the land on which it was built, the bridge being a mere extension of the highway over the river, it was held that, when the charter of the corporation expired by limitation, its franchise to take tolls terminated, and a right to the free use of the bridge vested in the public.316

Where the franchises of a corporation, however, as of a turnpike company, for example, have been transferred to an individual, under legislative authority, before dissolution of the corporation, the fact that the corporation has ceased to exist is immaterial, in an action by the transferee, as the real party in interest, for violation of the rights acquired under the transfer.317

## § 326. Effect of dissolution with respect to debts and contracts.

(a) In general.—The common-law rule was that, on the dissolution of a corporation, all the debts due either by or to the corporate body were extinguished, and this rule has been recognized in some of the cases in this country.318 For example, in a Delaware case it was held that, on the dissolution of a

316 State v. Lawrence Bridge mercial Bank v. Lockwood's Adm'r, 2 Har. (Del.) 8; Hightower v. Thornton, 8 Ga. 486, 52 Am. Dec. 412; Thornton v. Lane, 11 Ga. 459; Moultrie v. Smiley, 16 Ga. 289; Robinson v. Lane, 19 Ga. 337; Con-well v. Pattison, 28 Ind. 509; Town of Port Gibson v. Moore, 13 Smedes M. (Miss.) 157; Commercial charged with them, in their natural Bank of Natchez v. Chambers, 8 capacities; agreeable to that maxim of the civil law, 'si quid universitati debetur, singulis non debetur; nec, quod debet universitas, C.) 358, 36 Am. Dec. 48; Malloy v. singuli debent.'" 1 Bl. Com. 484. Mallett, 6 Jones, Eq. (N. C.) 345; See, also, Rider v. Nelson & Alberarle Union Factory, 7 Leigh Tiddy, 67 N. C. 169; White v. (Va.) 156, 30 Am. Dec. 495; Com-

Co., 22 Kan. 438.

<sup>317</sup> Clow v. Van Loan, 6 Thomp. & C. (N. Y.) 458.

<sup>318 &</sup>quot;The debts of a corporation, either to or from it," says Blackstone, "are totally extinguished by its dissolution; so that the members thereof cannot recover, or be & charged with them, in their natural Bank of Natchez v. Chambers, 8

corporation by the expiration of its charter, all the debts due to it were extinguished, and that it was not in the power of the legislature to revive the same by renewing its charter. 319

In most jurisdictions, however, if not in all, this doctrine no longer obtains. In many states it has been changed by statute,320 and, even in the absence of statutory provision, it has been held in the case of private business corporations that, while debts due to or by a corporation cannot be enforced at law after its dissolution, for want of a person to sue or be sued, they are not extinguished in equity; and that a court of equity, where no other remedy is provided by statute, will, by the appointment of a receiver, collect all debts which were due to the corporation at the time of its dissolution, or afterwards maturing, as a part of its assets, and apply its assets in payment of debts due by it.321

(b) Executory contracts.—According to the modern doctrine, liabilities of a corporation under executory contracts are not extinguished by its dissolution. This is undoubtedly true where the dissolution is voluntary, and some courts have applied the rule to involuntary dissolution. 322 In the nature of things, specific performance cannot be compelled by the other party, but he is entitled to damages for nonperformance, and such

wood's Adm'r, 2 Har. (Del.) 8.

320 See post, § 331 et seq. That the legislature has the power to abolish the common-law rule, see Robinson v. Lane, 19 Ga. 337; Commercial Bank of Natchez v. Chambers, 8 Smedes & M. (Miss.) 9; and cases hereafter cited. But see Commercial Bank v. Lockwood's Adm'r, 2 Har. (Del.) 8, note 319, supra.

321 Bacon v. Robertson, 18 How. (U. S.) 480, 2 Smith's Cas. 618, 1 Cum. Cas. 468; Curran v. State, 15 How. (U. S.) 310; Mumma v. Potomac Co., 8 Pet. (U. S.) 281, 2 Smith's Cas. 614, 1 Cum. Cas. 459; Lothrop v. Stedman, 13 Blatchf. man, 44 La. A 134, Fed. Cas. No. 8,519; Howe v. Blackwater B Robinson, 20 Fla. 352; Hargroves 46 W. Va. 56.

v. Chambers, 30 Ga. 580; McCoy v. Chambers, 30 Ga. 580; McCoy v. Farmer, 65 Mo. 244; People v. National Trust Co., 82 N. Y. 283; Heath v. Barmore, 50 N. Y. 302; Owen v. Smith, 31 Barb. (N. Y.) obinson v. Lane, 19 Ga. 337; Omercial Bank of Natchez v. Commercial Bank of Natchez v. Commercial Bank of Providence v. Commercial Bank of Bristol 68 v. Commercial Bank of Bristol, 68 v. Commercial Bank of Bristol, 68 Ill. 348; State v. Bank of Tennessee, 5 Baxt. (Tenn.) 101; Panhandle Nat. Bank v. Emery, 78 Tex. 498. See, also, National Pahquioque Bank v. First Nat. Bank of Bethel, 36 Conn. 325, 4 Am. Rep.

322 Shields v. Ohio, 95 U. S. 319, 324; People v. National Trust Co., 82 N. Y. 233; Schleider v. Diel-man, 44 La. Ann. 462; Griffith v. Blackwater Boom & Lumber Co.,

liability on the part of the corporation may be enforced in equity against the property of the corporation. 323 gations imposed by a lease to a corporation are not extinguished by its dissolution, unless the lease so provides, 324 and the obligation to pay rent, in accordance with the terms of the lease, may be enforced against its receiver. 325 Though a statute may confer upon a corporation the power to dissolve at will, the right to do so does not carry with it the power to impair the obligation of its contracts. In case of dissolution, the other party to an executory contract of the corporation cannot compel specific performance, but he has an equitable remedy for the recovery of damages.326

It is a settled principle that a contract is discharged and further performance excused, where further performance is rendered impossible by an act of the state, as by a change in the law, etc. And in accordance with this principle it was held in a New York case that, where a general agent of a life insurance company was engaged by the company for five years at a stipulated salary, but, before the expiration of the five years, the company was enjoined from doing business, and a receiver was appointed, in proceedings instituted by the state superintendent of the insurance department, and prosecuted by the attorney general, the contract of employment was discharged by the action of the state, and the agent had no claim upon the assets

In Weatherly v. Capital City Water Co., 115 Ala. 156, it was held that a decree of dissolution of statutory trustees of the company.

82 N. Y. 283.

A lease of a railroad to a corporation, to run for a term of years and "as long as it shall continue to exist as a corporation, and be capable of exercising its functions,"

323 Schleider v. Dielman, 44 La. means that the tenancy is to end only when there is legal disability to perform its contract, and not mere financial inability to perform, and, therefore, the lease is not tera water company did not abrogate minated by the mere appointment a contract with a city to supply it of a receiver for the lessee, to conwith water, and that the city might tinue until final judgment is eninsist upon a continued supply by tered, in an action by the attorney statutory trustees of the company, general to dissolve it for insol
324 People v. National Trust Co., vency. New York Elevated R. Co. v. Manhattan Ry. Co., 63 How. Pr. (N. Y.) 14.

325 People v. National Trust Co., 82 N. Y. 283.

326 Schleider v. Dielman, 44 La. Ann. 462.

of the company in the receiver's hands for damages for alleged breach of the contract.327 And in an early Virginia case, it was held that, although there was no express order for the removal of a person employed as professor in a college, yet, where the college was discontinued by statute, the employment or office, together with the salary pertaining thereto, also ceased.328 In a late New Jersey case, however, there was a decision to the contrary. It was there held that the dissolution of a corporation having a capital stock, by a judgment in proceedings to forfeit its charter, did not discharge a contract by which a person was employed by the corporation for a term, and that he could enforce his claim for damages for the term of his contract unexpired at the time of the forfeiture.329

In some jurisdictions, statutes have been enacted authorizing the transfer of choses in action by a corporation on the expiration of its charter. Under such a statute, an assignment by a corporation of a note given for the price of land, together with a deed thereto, carries the right to keep up and make good a tender by delivery of the deed.330

(c) Contracts after dissolution .- In the nature of things, a corporation cannot, any more than a dead person, become a party to a note or any other contract after it has been dissolved.831 Thus it has been held that a note executed to a corporation after its dissolution is absolutely void for want of a payee.<sup>332</sup> A corporation, however, may contract after commencement of proceedings to forfeit its charter, but before a forfeiture is finally declared. Thus it may execute a bond in order to appeal or sue out a writ of error from or to a judgment forfeiting its charter, and the bond will be valid although the

<sup>327</sup> People v. Globe Mutual Life Credit System Co., 61 N. J. Law, Ins. Co., 64 How. Pr. (N. Y.) 240, 543, reversing 60 N. J. Law, 294. 91 N. Y. 174. And see Griffith v. 330 Bank of Salem v. Caldwell, Blackwater Boom & Lumber Co., 16 Ind. 469. 46 W. Va. 56.

<sup>328</sup> Bracken v. William & Mary College, 1 Call (Va.) 161.

<sup>329</sup> Rosenbaum v. United States (Tenn.) 38.

<sup>331</sup> Saltmarsh v. Planters' & Merchants' Bank, 14 Ala. 668; White v. Campbell, 5 Humph. (Tenn.) 38. 332 White v. Campbell, 5 Humph.

judgment is affirmed, for until the affirmance there is no dissolution.333

- (d) Offer before and acceptance after dissolution.—If a corporation should be dissolved after an offer has been made by it to enter into a contract, and before its acceptance, the offer would undoubtedly lapse, and would be no longer open for acceptance, just as an offer lapses upon the death or insanity of a natural person by whom it is made,384 or upon the dissolution of a partnership by which it is made, to the knowledge of the other party.335
- (e) Liability of stockholders or members.—Stockholders or members of a corporation who participate in or authorize the continuance of business under the corporate name after the expiration of its charter, or its dissolution by forfeiture or otherwise, are liable as partners on all contracts made in the course Thus, in a New York case, where the stockof such business. holders in a manufacturing corporation, on the expiration of its charter, agreed to continue the business, appointed a managing agent, and agreed to furnish money when called upon by him to carry on the business, in proportion to the amount of stock held by each in the corporation, and the agent made commercial paper in the name of the corporation, by himself as agent, it was held that there was a partnership, and that all the members of the association were liable on the paper to its full amount, 336

The effect of dissolution with respect to the statutory liability of stockholders, and the rights of creditors thereafter, is considered in a subsequent chapter.\*

333 Texas Trunk Ry. Co. v. Jackson, 85 Tex. 605. And see Giles v. Holfenstein's Estate, Stanton, 86 Tex. 620; ante, § 324. 328, 18 Am. Rep. 449.

334 Wallace v. Townsend, 43 Ohio St. 537, 54 Am. Rep. 829; Mactier's Adm'r v. Frith, 6 Wend. (N. Y.) 103, 21 Am. Dec. 262; Pratt v. Trustees of Baptist Society of El-

gin, 93 Ill. 475, 34 Am. Rep. 187: Holfenstein's Estate, 77 Pa. St.

335 Goodspeed v. Wiard Plow Co., 45 Mich. 322.

836 National Union Bank of Watertown v. Landon, 45 N. Y. 410.

\*See post, chapter xxv.

### § 327. Effect of dissolution with respect to torts.

At common law, a right of action against a corporation for a tort does not survive its dissolution, but it is otherwise under a statute providing that the dissolution of a corporation shall not impair any remedy against it or its officers for liabilities previously incurred.387 or under a statute providing that, on the dissolution of a corporation, the directors shall be trustees for the "creditors" and stockholders, with full power to settle the affairs of the corporation.338

It was held in a West Virginia case that a private business corporation which failed to wind up its business when its charter expired, and continued to do business in the corporate name, might be sued for a tort committed after expiration of its charter, on the ground that it was a corporation de facto. 339 the weight of authority, however, as was shown in a previous section, a corporation has not even a de facto corporate existence after expiration of its charter; 340 and where this is the case, such an action could not be maintained. The only remedy would be against the individuals committing the wrong.

## § 328. Effect of dissolution with respect to property and conveyances.

(a) In general.—It has repeatedly been said by text writers and judges, and has been directly held in some of the cases, that, at common law, upon the dissolution of a corporation, all its real estate reverted to the grantors or donors or their heirs, and all its personal estate escheated to the king, or, in this country, to the state; and in some late cases this doctrine has been applied in this country, in equity as well as at law, to

62 Hun (N. Y.) 257; People v. Troy Steel & Iron Co., 82 Hun (N. Y.) 303. See, post, § 333(b). 339 Miller v. Newburg Orrel Coal

vived the dissolution of the corpo- Co., 31 W. Va. 836, 13 Am. St. Rep.

Y. 398.

340 Bradley v. Reppell, 133 Mo.

388 Marstaller v. Mills, 143 N. Y. 545, 54 Am. St. Rep. 685; ante, §
398; Hepworth v. Union Ferry Co., 82(c)(4).

<sup>337</sup> Under such a statute in New York, it was held that a right of action against a corporation for personal injuries to one's son surration. Marstaller v. Mills, 143 N. 903.

some kinds of corporations. It is very doubtful, however, whether there is any real authority for the doctrine that the real estate of a corporation reverts to the donors or grantors. or their heirs.341

In a comparatively late Maine case, the doctrine, in so far as personal estate was concerned, was applied to a mutual insurance company, which, after its last policy had expired, voted to discontinue business and wind up its affairs, and obtained a decree of dissolution. As there were no stockholders among whom the assets could be distributed under the statute, it was held that the common-law rule applied, and that the assets vested in the state.342

The rule has also been held to be applicable to charitable and religious corporations and the like, both as to real and personal estate.343 In a late case in the supreme court of the United States it was held that, on the repeal by congress of the charter of the Mormon corporation, known as the "Church of Jesus Christ of Latter-Day Saints," chartered by the territory of Utah, all its real estate, which was de-

Fassett, 102 III. 315; Mott v. Dan- Law Rev. 135. ville Seminary, 129 III. 403; Danville Seminary v. Mott, 136 III. 289; Late Corporation of Church of Jesus Christ of Latter-Day Saints v. United States, 136 U.S. 1.

statement of Lord Coke. Co. Litt. Saints v. United States, 136 U. S. 13b. Professor Gray, however, in 1; People v. Trustees of College of his work on the "Rule against Per-California, 38 Cal. 166; Mott v. petuities," expresses doubt as to Danville Seminary, 129 Ill. 403; its soundness, pointing out that the Danville Seminary v. Mott, 136 Ill. only justification for Lord Coke's 289.

341 The doctrine has been laid assertion is a mere dictum of down or applied in the following Choke, J., in the Prior of Spaldtext books and cases: Co. Litt. ing's Case, 7 Edw. IV. 10-12. Gray, 13b; 1 Bl. Com. 484; 2 Kent, Perpetuities, §§ 44-48. It is re-Com. 385; White v. Campbell, 5 ferred to in a note in the Harvard Humph. (Tenn.) 38; People v. Law Review, on the authority of Trustees of College of California, Professor Gray, as "the long prev-38 Cal. 166; Owen v. Smith, 31 alent but erroneous notion that Barb. (N. Y.) 645; Titcomb v. real estate remaining unsold at the Kennebunk Mutual Fire Ins. Co., dissolution or civil death of a cor-79 Me. 315, 1 Cum. Cas. 476; State poration reverts to the original v. Lawrence Bridge Co., 22 Kan. grantor or his heirs," and as "this 438; Life Association of America v. time-honored delusion." 3 Harv.

> 342 Titcomb v. Kennebunk Mutual Fire Ins. Co., 79 Me. 315, 1 Cum. Cas. 476.

343 Late Corporation of Church This doctrine is based upon a of Jesus Christ of Latter-Day rived by it from the United States under act of congress, and was held by individuals in trust for the corporation, reverted to the United States, and also that its personal estate escheated to the United States, to be applied either by congress or by the court under the cy pres doctrine to some object of a like kind.

It was said in this case by Mr. Justice Bradley: "When a business corporation, instituted for the purposes of gain, or private interest, is dissolved, the modern doctrine is, that its property, after payment of its debts, equitably belongs to its stockholders. But this doctrine has never been extended to public or charitable corporations. As to these, the ancient and established rule prevails, namely: that when a corporation is dissolved, its personal property, like that of a man dying without heirs, ceases to be the subject of private ownership, and becomes subject to the disposal of the sovereign authority; whilst its real estate reverts or escheats to the grantor or donor, unless some other course of devolution has been directed by positive law, though still subject \* \* \* to the charitable use."344

(b) The rule in equity applicable to modern business corporations.—This rule, however, does not apply in equity to modern business corporations. On the dissolution of such a corporation, whether by expiration of its charter, by a judgment of forfeiture, or otherwise, it is considered in equity, even in the absence of any statute, that its assets are held for the benefit of its steckholders or members, after payment of its debts, and it will be so distributed by a court of equity when no other mode of distribution is provided by statute.345

The equitable right of creditors of a dissolved corporation

s44 Late Corporation of Church Superior Court, 84 Cal. 327, 18 Am. of Jesus Christ of Latter-Day St. Rep. 192; Wilson v. Leary, 120 Saints v. United States, 136 U. S. 1, 47.

345 Bacon v. Robertson, 18 How. 641; Towar v. Hale, 46 Barb. (N. (U. S.) 480, 2 Smith's Cas. 618, 1 Y.) 361; Heath v. Barmore, 50 N. Cum. Cas. 468; State v. Commercial State Bank, 28 Neb. 677, 2 Co., 82 N. Y. 283; Heman v. Brit-Smith's Cas. 616; People v. ton, 88 Mo. 549; Moore v. Willa-O'Brien, 45 Hun (N. Y.) 519, 111 mette Transportation & Locks Co., N. Y. 1, 7 Am. St. Rep. 684, 2 7 Or. 359; Hightower v. Thorn-Smith's Cas. 728; Havemeyer v. ton, 8 Ga. 486, 52 Am. Dec. 412;

to have its assets applied to the satisfaction of their claims is superior to any rights of the stockholders, or of their assignces. When a corporation is dissolved, its assets are a trust fund for the payment of its debts, and will be applied for this purpose by a court of equity, before any distribution among the stock-And it necessarily follows that the rights of creditors of a dissolved corporation in the distribution of its assets are superior to the rights of the individual creditors of stockholders.347

- (c) Statutory provisions for winding up.—In most jurisdictions, if not in all, in order to give effect to the equitable rule above mentioned, express statutory provision has been made for the winding up of corporations on their dissolution, and the distribution of their property to the stockholders, after payment of their debts, either by making the officers of the corporation trustees for such purpose, or by continuing the existence of the corporation for a certain period for such purpose, or by providing for the appointment of a receiver. These statutes will be considered in a subsequent section.348
- (d) Transfer or assignment before dissolution.—It is obvious that a transfer or assignment of its property by a corporation, before dissolution, if valid, is not affected by its subsequent dissolution, from whatever cause. And it can make no difference that the transfer or assignment is in trust for the benefit of creditors, or stockholders, or both.349

Where the directors of a corporation, just before its charter expires, transfer its property to trustees for the benefit of the stockholders, the title to the property will not be affected by

State v. Bank of Tennessee, 5 Cum. Cas. 468; State v. Commer-Baxt. (Tenn.) 101; Fleitas v. City of New Orleans, 51 La. Ann. 1.

Stockholders and creditors of a corporation may maintain a suit in equity after its dissolution to recover assets wrongfully appropriated or withheld, and to have them applied for their benefit. Boyd v. Hankinson (C. C. A.) 92 Fed. 49.

cial State Bank, 28 Neb. 677, 2 Smith's Cas. 616.

347 State v. Commercial State Bank, 28 Neb. 677, 2 Smith's Cas.

348 Post, § 331 et seq.

349 See Bailey v. Platte & Denver ankinson (C. C. A.) 92 Fed. 49. Canal & Milling Co., 12 Colo. 230; 346 Bacon v. Robertson, 18 How. Leach v. Thomas, 27 Ill. 457; and (U. S.) 480, 2 Smith's Cas. 618, 1 cases cited in the notes following. the expiration of the charter, and consequent dissolution of the corporation, for the title of the corporation ceases on the transfer, and the legal title vests in the trustees, with the beneficial interest in the stockholders.350 So, if a corporation, before the expiration of its charter, assigns its choses in action to a trustee for the use of its stockholders, the assignment is not affected by its dissolution on expiration of its charter, and, after such dissolution, the trustee may maintain actions in his own name.351

Where a corporation makes an assignment for the benefit of its creditors before the expiration of its charter, the rights of the assignees under it cannot be affected by that event.352

Where a mortgage or deed of trust executed by a corporation. to secure the payment of bonds issued by it, authorizes the trustees, in default of payment of the principal or interest, to take possession of the mortgaged property, and to borrow money necessary to preserve, protect, and operate it, making the amount so borrowed a charge upon the proceeds of a sale of the property, such provisions secure a property right or interest which survives a dissolution of the corporation at the instance of stockholders, by virtue of a statute, and the powers may be exercised by the trustees after such dissolution.353

Where a corporation, while in existence, indorses and transfers notes held by it, the subsequent expiration of its charter cannot affect the rights of the indorsee, or deprive him of the right to sue the maker of the notes.354

A judgment in favor of a corporation, if properly assigned, may be enforced after the corporation has been dissolved by expiration of its charter or otherwise.355

(e) Conveyance to or by corporation after dissolution.—Of course a corporation cannot take or make a conveyance of prop-

350 Stevens v. Hill, 29 Me. 133. And see Folger v. Chase, 18 Pick. 1 Rob. (Va.) 524. (Mass.) 63.

351 Cooper v. Curtis, 30 Me. 488. And see Folger v. Chase, 18 Pick. (Mass.) 66. (Mass.) 63.

352 Bank of Alexandria v. Patton,

353 Nelson v. Hubbard, 96 Ala. 238, 254,

354 Folger v. Chase, 18 Pick.

355 Leach v. Thomas, 27 III. 457.

erty after its dissolution.356 In the absence of a statute, however, there must be, not merely liability to dissolution, but actual dissolution. Where a corporation took a conveyance of property after the legislature had passed an act providing for a forfeiture of its charter and dissolution, but before proceedings to enforce the forfeiture, it was held that it had the power to take and hold the same, and there can be no doubt that it could have conveyed the same before actual dissolution.358

(f) Conveyance in trust for corporation.—Since a dissolved corporation no longer exists for any purpose, property cannot be conveyed in trust for the use of a corporation after it has been dissolved. Thus, where a note secured by a deed of trust is executed to a defunct corporation, not only is the note void for want of a payee, but the deed of trust is also void for want of a beneficiary.359

# Effect of dissolution with respect to actions and proceed-§ 329.

In the absence of statutory provision to the contrary, a corporation, after it has been legally dissolved, can neither sue nor be sued, and all actions or proceedings commenced against it prior to its dissolution are abated.360 There are a few deci-

545, 54 Am. St. Rep. 685. See Ala. 472; Nelson v. Hubbard, 96 White v. Campbell, 5 Humph. Ala. 238. (Tenn.) 38; Montgomery v. Merrill, 18 Mich. 338.

357 See ante, § 313.

(Tenn.) 38.

360 United States: Mumma v. Potomac Co., 8 Pet. 281, 2 Smith's Cas. 614, 1 Cum. Cas. 459; Selma First Nat. Bank v. Colby, 21 Wall. 609; Pendleton v. Russell, 144 U. S. 645; Dundee Mortgage & Trust Inv. Co. v. Hughes, 77 Fed. .855; Greeley v. Smith, 3 Story, 657, Fed. Cas. No. 5,748.

Alabama: Saltmarsh v. Planters' & Merchants' Bank of Mobile, 17

356 Bradley v. Reppell, 133 Mo. Ala. 761; Paschall v. Whitsett, 11

Connecticut: National Pahquioque Bank v. First Nat. Bank of Bethel, 36 Conn. 325, 334, 4 Am. 358 Montgomery v. Merrill, 18 Rep. 80; Wilcox v. Continental Life Ins. Co., 56 Conn. 468; Morgan v. 359 White v. Campbell, 5 Humph. New York National Building & Loan Ass'n, 73 Conn. 151.

Delaware: Commercial Bank v. Lockwood's Adm'r, 2 Har. 8.

Florida: Howe v. Robinson, 20

Georgia: Terry v. Merchants' & Planters' Bank of Savannah, 66 Ga. 177; Hightower v. Thornton, 8 Ga. 486, 52 Am. Dec. 412; Carey v. Giles, 10 Ga. 9.

Illinois: City Ins. Co. of Providence v. Commercial Bank of Brissions to the contrary, 361 but this rule is supported by an overwhelming weight of authority. Where a corporation was duly dissolved in a manner provided by its charter and the state statutes, it was held that the dissolution abated a suit by a stockholder in a federal court for an injunction against the business carried on by the corporation, and the appointment of a receiver, on the ground that the business was ultra vires.362

Attachment.—There can be no attachment for debt against a

tol. 68 Ill. 348: Life Association of America v. Fassett, 102 Ill. 315.

Iowa: Muscatine Turn Verein v. Funck, 18 Iowa, 469, 473; District of Clay v. District of Buchanan, 63 Iowa, 188.

Kansas: Eagle Chair Co. v. Kel-

sey, 23 Kan. 632.

Louisiana: Bank of Louisiana v.

Wilson, 19 La. Ann. 1; Musson v. Richardson, 11 Rob. 37.
Maine: Merrill v. Suffolk Bank, 31 Me. 57, 50 Am. Dec. 649; Bowker v. Hill, 60 Me. 172; Rankin v. Sherwood, 33 Me. 509.

Massachusetts: Thornton v. Marginal Freight Ry. Co., 123 Mass. 32,

1 Cum. Cas. 462.

Mississippi: Bank of Mississippi v. Wrenn, 3 Smedes & M. 791; Town of Port Gibson v. Moore, 13 Smedes & M. 157.

New York: McCulloch v. Norwood, 58 N. Y. 562; Sturgis v.

Drew, 11 Hun, 136.

North Carolina: Dobson v. Simonton, 86 N. C. 492; Fox v. Horah, 1 Ired. Eq. 358, 36 Am. Dec.

Miami Exporting Co. v.

Gano, 13 Ohio, 269.

Pennsylvania: Farmers' & Mechanics' Bank v. Little, 8 Watts & S. 207, 42 Am. Dec. 293; Cooper v. Oriental Savings & Loan Ass'n, 100 Pa. St. 402; Building Association v. Anderson, 7 Phila. 106; Houston v. Jefferson College, 63 Pa. St. 428.

Rhode Island: Insurance Commissioner v. United Fire Ins. Co.,

Tennessee: Ingraham v. Terry, 11 Humph, 572; White v. Campbell, 5 Humph. 38.

Texas: Life Association of America v. Goode, 71 Tex. 90.

Virginia: Rider v. Nelson & Albemarle Union Factory, 7 Leigh, 156, 30 Am. Dec. 495; May v. State Bank of North Carolina, 2 Rob. 56, 40 Am. Dec. 726.

West Virginia: Stiles v. Laurel Fork Oil & Coal Co., 35 S. E. 986. Wisconsin: Combes v. Keyes, 89

As to the effect of consolidation upon actions by or against the consolidating corporations, see post,

"I cannot distinguish," said Mr. Justice Story, "between the case of a corporation and the case of a private person, dying pendente lite. In the latter case, the suit is abated at law, unless it is capable of being revived by the enactments of some statute, as is the case as to suits pending in the courts of the United States, where, if the right of action survives, the personal representative of the deceased party may appear, and prosecute or defend the suit. No such provision exists as to corporations; nor, indeed, could exist, without reviving the corporation pro hac vice; and therefore, any suit pending against it at its death abates by mere operation of law." Greeley v. Smith, 3 Story, 657, Fed. Cas. No. 5,748.

361 Kansas City Hotel Co. v. Sauer, 65 Mo. 279; Lindell v. Benton, 6 Mo. 361; Evans v. Inter-state Rapid Transit Ry. Co., 106 Mo. 594; Butchers' & Drovers' Bank v. Pulitzer, 11 Mo. App. 594.

362 Lang v. Louisiana Tanning Co., 56 Fed. 675.

corporation whose charter has expired or been forfeited. And it has also been held that the dissolution of a corporation by expiration of its charter or a decree of forfeiture of its charter rendered pending attachment proceedings against it as defendant, and before judgment therein, dissolves the attachment. 363

Judgment and execution .- A judgment rendered against a corporation after its dissolution, though the action may have been brought before, is absolutely void, in the absence of statutory provision to the contrary, just as a judgment rendered against a natural person after his death is void, and it is subject, therefore, to collateral attack.364 And if, after a judgment is rendered in favor of or against a corporation, the corporation is dissolved by expiration of its charter, or otherwise, no execution on the judgment can be sued out in the name of the corporation, or against it, as the case may be.365 been held, however, that if an officer has levied upon or seized property on an execution in favor of or against a corporation, he may proceed with the execution of the writ by a sale of the

v. Little, 8 Watts & S. (Pa.) 207, Fassett, 102 Ill. 315; Combes v. 42 Am. Dec. 293; Frailey v. Cen-Keyes, 89 Wis. 297, 46 Am. St. tral Fire Ins. Co., 9 Phila. (Pa.) Rep. 839. And see Rankin v. 219; Wilcox v. Continental Life Sherwood, 33 Me. 509. Contra, Ins. Co., 56 Conn. 468; Morgan v. Kansas City Hotel Co. v. Sauer, New York National Building & 65 Mo. 279, and other Missouri Loan Ass'n, 73 Conn. 151; Stiles cases cited in note 361, supra. v. Laurel Fork Oil & Coal Co. (W. Va.) 35 S. E. 986.

Compare Hays v. Lycoming Fire Ins. Co., 99 Pa. St. 621; Life Association of America v. Fassett, 102 Ill. 315; Lindell v. Benton, 6 Mo. 361. And see People v. Mutual Benefit Life Ass'n of America, 86

Hun (N. Y.) 219. 364 Dobson v. Simonton, 86 N. C. 492; Thornton v. Marginal Freight Ry. Co., 123 Mass. 32, 1 Cum. Cas. 462; Mumma v. Potomac Co., 8 Pet. (U. S.) 281, 2 Smith's Cas. 614, 1 Cum. Cas. 459; Merrill v. Suffolk Bank, 31 Me. 57, 50 Am. Dec. 649; Sturges v. Vanderbilt, 73 N. Y. 384; District of Clay v. District of Buchanan, 63 Iowa, 188; Leach v. Thomas, 27 III, 457.

After the charter of a corporation has been forfeited, and its assets are in the hands of a receiver. a judgment rendered against the corporation is absolutely void, although it may have been rendered by consent of counsel. Insurance Commissioners v. United Fire Ins. Co. (R. I.) 48 Atl. 202.

365 May v. State Bank of North Carolina, 2 Rob. (Va.) 56, 40 Am. Dec. 726; Kimball v. Grafton Bank, 20 N. H. 347; Boyd v. Hankinson, 83 Fed. 876.

The judgment may be enforced, however, if it has been properly assigned before the dissolution. property, although the corporation may have been dissolved since the levy or seizure.366

Scire facias.—According to this doctrine, a writ of scire facias to revive a judgment rendered against a corporation before its dissolution cannot be maintained after its dissolution. nor can a judgment of revival be entered after dissolution on a writ issued before dissolution.367 Nor can a corporation, after its dissolution, maintain scire facias to enforce a mortgage.368

Appeal and writ of error.—Ordinarily an appeal or writ of error from or to a judgment for or against a corporation cannot be prosecuted in the name of the corporation after its existence has expired;369 but it has been held that, where the rights of a corporation whose existence has terminated pending an appeal or writ of error from or to a judgment or decree in favor of or against it have passed to others by assignment for value during its existence, the case may proceed to judgment or decree in the appellate court. 370 Where a corporation appeals from a judgment forfeiting its charter, and the judgment is affirmed, it is not dissolved until the affirmance, and therefore a judgment rendered against it after the judgment appealed from, but before its affirmance, is valid.371

Bankruptcy proceedings.—State laws on the subject of insolvency and bankruptcy must yield to the federal bankruptcy law in so far as they conflict; and it has been held, therefore, that a corporation may be proceeded against in bankruptcy under the federal bankruptcy law, notwithstanding a decree of a state court under a state law dissolving it and appointing a receiver.372

876, (C. C. A.) 92 Fed. 49; Kimball v. Grafton Bank, 20 N. H. 347.

367 Mumma v. Potomac Co., 8 Pet. (U. S.) 281, 2 Smith's Cas. ton, 1 Rob. (Va.) 499. 614, 1 Cum. Cas. 459; Howe v. 371 Giles v. Stanton, Robinson, 20 Fla. 352.

368 Cooper v. Oriental Savings & Loan Ass'n, 100 Pa. St. 402; Build-

366 Boyd v. Hankinson, 83 Fed. v. Fassett, 102 Ill. 315. Under statutory provisions, see note 399, infra.

370 Bank of Alexandria v. Pat-

371 Giles v. Stanton, 86 Tex. 620. And see Texas Trunk Ry. Co. v. Jackson, 85 Tex. 605; ante, § 324. 372 Platt v. Archer, 9 Blatchf. ring Association v. Anderson, 7 559, Fed. Cas. No. 11,213; In re Phila. (Pa.) 106. Independent Ins. Co., 1 Holmes, 369 Life Association of America 103, Fed. Cas. No. 7,017.

Statutory provisions .- Because of the common-law rule preventing actions by or against a corporation after its dissolution. the only remedy for the protection of the rights of stockholders and creditors was by resort to a court of equity; but in most jurisdictions, the difficulty has been obviated by statutory provisions, either continuing the existence of corporations for a certain period after expiration of their charter, for the purpose of allowing them to gradually wind up their affairs, and to sue and be sued, or by making the officers trustees for the creditors and stockholders, and allowing suits by and against them, or by providing for the appointment of a receiver, and allowing suits by and against him. 373 These statutes will be considered to better advantage in a subsequent section.<sup>374</sup>

An action may be brought against a corporation after its dissolution by repeal of its charter on a debt previously incurred, where there is a statutory provision that no repeal by the legislature of the charter of any corporation "shall take away or impair any remedy given against such corporation, its members or officers, for any liability which shall have been previously incurred."375 And a suit commenced against a corporation before the repeal of its charter may be prosecuted to judgment after such repeal, where a statute provides that "the repeal of any act shall in no case affect any act done, or any right accruing, accrued, acquired or established, or any suit or proceeding had or commenced in any civil case, before the time when said repeal shall take effect."376

v. Callender, 20 Ohio St. 190; Richmond Union Passenger Ry. Co. v. New York & Sea Beach Ry. Co., 95 Va. 386; Wehn v. Fall, 55 Neb. 547; Schmidt Bros. Co. v. Mahoney, 60 Neb. 20.

<sup>374</sup> Post, §§ 331-334.

<sup>375</sup> Blake v. Portsmouth & Concord Railroad, 39 N. H. 435.

<sup>373</sup> Stetson v. City Bank of New corporation after its dissolution, on Orleans, 2 Ohio St. 167; Warner a cause of action which arose before, is valid, where a statute provides that the dissolution of a corporation for any cause shall not take away or impair any remedy given against such corporation for liabilities incurred previous to its dissolution. Steinhauer v. Colmar, 11 Colo. App. 494.

<sup>376</sup> Blake v. Portsmouth & Con-A judgment rendered against a cord Railroad, 39 N. H. 435.

## § 330. Effect of dissolution on transfer of stock.

Though the dissolution of a corporation can have no effect upon prior transfers of shares of its stock, shares of stock in a corporation cannot be transferred, so as to pass the legal title, after the corporation has been dissolved, for the transferable nature of the stock is destroyed by the dissolution; but a sale of stock after the dissolution will transfer the right of the seller to any balance of assets which may be found to be due him after payment of his debts to the corporation.<sup>377</sup>

Where shares of stock have been duly transferred upon the books of a corporation before its dissolution by a decree of court, or otherwise, and nothing remains to be done except the ministerial act of the treasurer's affixing his signature to the certificate of shares, so as to thereby make the evidence of the transferee's title, the signature may be affixed after the dissolution of the corporation. Such an act involves the exercise of no corporate act or power, but is merely the formal authentication of that which in substance and legal effect has been executed before the dissolution.<sup>378</sup>

# V. CONTINUANCE AND WINDING UP OF CORPORATIONS UNDER STATUTORY PROVISIONS.

§ 331. In general.—In most jurisdictions, if not in all, the legislatures have expressly provided by statute for the winding up of the business of corporations on their dissolution, whether by the expiration of their charter, or by judgment of forfeiture, or otherwise, either by providing for the appointment of receivers or trustees to collect and distribute their assets, or by making their officers trustees for creditors and stockholders, or, in case of the expiration or annulment of their charter, by continuing their existence for a certain period for the purpose of allowing them to act in their corporate capacity in winding up their affairs and distributing their assets. Such statutes, as we have seen, are not unconstitutional.<sup>379</sup>

<sup>377</sup> James v. Woodruff, 10 Paige 379 Foster v. Essex Bank, 16 (N. Y.) 541, 2 Denio, 574. Mass. 245, 8 Am. Dec. 135, 2 378 Sewall v. Chamberlain, 16 Gray (Mass.) 581. Smith's Cas. 608, 1 Cum. Cas. 464; Mumma v. Potomac Co., 8 Pet.

#### § 332. Continuance of existence of corporations.

(a) In general.—In a number of states it is expressly provided that corporations, upon the expiration or annulment of their charter, shall continue in existence for a specified period, or sometimes indefinitely, 380 for the purpose of gradually winding up their affairs, disposing of their property, suing and being sued, and dividing their assets. 381 Sometimes such a provision is found in the special charter of a corporation, or in the general law under which a corporation is organized, but more frequently it is a general provision applicable to all corpora-

A provision in an incorporation law, allowing corporations created under it a certain period for winding up their affairs, enters into and is a part of the charter of every corporation organized under it.382 And corporations organized under stat-

Cum. Cas. 459; Franklin Bank v. poration has ceased by the expira-Cooper, 36 Me. 179; Cooper v. tion of the time limited in its Curtis, 30 Me. 488; Nevitt v. Bank charter, and the rights of creditors of Port Gibson, 6 Smedes & M. and stockholders have expired by (Miss.) 513; Tuskaloosa Scientific such extinction, the legislature has

In Georgia it has been held that, since Code, § 1679, declares that all corporations have the right to sue and be sued, to have and use a common seal, to make by-laws, to receive donations, to purchase and hold property necessary for the purpose of their organization, and to do all acts necessary for the legitimate execution of this purpose, the legislature cannot hinder the charter of a business corporation from expiring, and the corporation from being dissolved, by enacting a special law declaring that the charter be continued in force only for the purpose of terminating suits and litigation pending against it; that provisions applicable alike to all corporations under the general law must remain applicable to each until changed by the general law. Logan v. Western & Atlantic R. Co., 87 Ga. 533.

And in Mississippi it was held

(U. S.) 281, 2 Smith's Cas. 614, 1 that where the existence of a cor-& Art Ass'n v. Green, 48 Ala. 346. no power to revive the corporation, and authorize it to collect claims due to it. Bank of Mississippi v. Duncan, 56 Miss. 166.

> 380 See Nashville Bank v. Petway, 3 Humph. (Tenn.) 522.

381 See Foster v. Essex Bank, 16 Mass. 245, 8 Am. Dec. 135, 2 Cum. Cas. 608, 1 Cum. Cas. 464; Herron v. Vance, 17 Ind. 595; Hanan v. Sage, 58 Fed. 651 (Minnesota statute); Cunningham v. Clark, 24 Ind. 7; Tuskaloosa Scientific & Art Ass'n v. Green, 48 Ala. 346; Saltmarsh v. Planters' & Merchants' Bank, 14 Ala. 668; Franklin Bank v. Cooper, 36 Me. 179; Mariners' Bank v. Sewall, 50 Me. 220; Pomeroy's Lessee v. Indiana Bank, 1 Wall. (U. S.) 23; Boyd v. Hankinson (C. C. A.) 92 Fed. 49; Farmers' Nat. Bank of Owatonna v. Backus, 74 Minn. 264; and cases specifically cited in the notes following.

382 Ferguson v. Miners' & Man-

utes authorizing the formation of particular kinds of corporations, as banking corporations, for example, are within a provision in a general incorporation act continuing the existence of corporations for the purpose of winding up their affairs.383

Where the charter of a corporation, limiting its existence to a certain number of years, provides that after the expiration of such period its powers and obligations shall continue (without limitation as to time) for the purpose of settling and winding up its affairs, and the charter is extended by a subsequent enactment for a certain period, the provision for continuance of the corporation after expiration of its charter, for the purpose of winding up its affairs, continues it indefinitely for such purpose after expiration of the period of extension.<sup>384</sup>

Where a statute provides that on dissolution of a corporation by limitation, forfeiture, or otherwise, its corporate capacity shall continue for a certain time for the purpose of settling up its affairs, conveying its property, and prosecuting or defending suits, the corporation itself becomes a trustee for its creditors and stockholders.385

Such statutes only apply where the circumstances are such as to bring the corporation within their provisions. Thus, a statute providing that corporations whose charters "have expired

ufacturers' Bank, 3 Sneed (Tenn.)

A statute continuing all corporations whose charters "may have expired" for two years, for the purpose of collecting their debts, and winding up their affairs, etc., is not restricted to existing corporations. but applies also to corporations afterwards organized. Singer v. Hutchinson, 83 Ill. App. 675, 183 III. 606.

In New Jersey, a corporation which has defaulted in the payment of taxes, and has been proclaimed by the governor under the act of April 21, 1896, thereby making its charter void, and the attempted exercise of powers under the charter a misdemeanor, has the Feeding Co., 73 Fed. 44 (under the power to wind up and settle the Illinois statute).

its affairs, as allowed by the corporation act of 1896. American Surety Co. v. Great White Spirit Co., 58 N. J. Eq. 526.

383 Cunningham v. Clark, 24 Ind. 7; Herron v. Vance, 17 Ind. 595.

An act continuing the existence of all corporations whose charters "may have expired" for a certain period, for the purpose of winding up their business, applies to corporations subsequently organized. Singer v. Hutchinson, 183 Ill. 606, 75 Am. St. Rep. 133, affirming 83 Ill. App. 675.

or been annulled" shall continue as bodies corporate for the purpose of winding up their business, etc., does not apply to a corporation whose charter has neither expired nor been annulled, but which has merely closed up its business and settled with its members.386

(b) Collection of debts.—When a statute continues the existence of a corporation after expiration or forfeiture of its charter for the purpose of allowing the collection of debts due to it.—and authority to collect debts is included in authority to wind up its business,—the statute should receive a liberal construction, so as to enable it to resort to all the usual and appropriate modes of securing the ultimate collection of its demands.387 Where an act accepting the surrender of the charter of a bank continued its corporate powers for the collection of debts then due, it was held that it was within the scope of its authority to take a new note in payment of one then held by it, although the indorsers of the two notes were not the same. 388 And where the existence of a bank was continued by statute for three years after expiration of its charter, for the purpose of settling its business, it was held that it was authorized, immediately before the expiration of the three years, to indorse a note held by it to trustees appointed to wind up its affairs, and who were vested by it with all its powers.<sup>389</sup>

Code, § 1690, providing that all suit, pay debts of the corporation corporations whose powers expire by limitation, and which are "dissolved by forfeiture or any other cery where their genuineness is questioned, and distribute among cause," shall exist for five years the stockholders such assets as thereafter for the purpose of "prosecuting or defending suits, settling their business, disposing to qualify and accept the appoint of their property, and dividing ment. Nelson v. Hubbard, 96 Ala. thorize a suit to foreclose a mortthorize a suit to foreclose a mortgage against a corporation which chants' Bank, 14 Ala. 668; Marhas been dissolved on the petition iners' Bank v. Sewall, 50 Me. 220. of a majority of its stockholders 388 Ma owning more than three-fourths of Me. 220. the stock, under Code, § 1683 et 389 Folger v. Chase, 18 Pick. seq., since provision is therein (Mass.) 63. See, also, Hanan v.

<sup>386</sup> Heggie v. People's Building made for the appointment of a re-& Loan Ass'n, 107 N. C. 581. ceiver to wind up the affairs of In Alabama it has been held that the corporation, collect debts by Code, § 1690, providing that all suit, pay debts of the corporation

387 Saltmarsh v. Planters' & Mer-

388 Mariners' Bank v. Sewall, 50

- (c) Engaging in new business.—But such a statute does not authorize it to engage in any new business transactions. Thus, where an act declares the charter of a bank forfeited, but authorizes its officers or trustees to use the corporate name in the collection of debts, and winding up of its business, the bank cannot discount or purchase a bill of exchange as a business transaction. 390
- (d) Power to hold property.—Under a statute providing that corporations whose charters have expired or been annulled may continue to act for the purpose of winding up their affairs, a corporation whose charter has expired or been annulled is entitled to hold property until its affairs are closed up.<sup>391</sup>
- (e) Disposal of property.—In winding up its business under such a statute, the majority of the stockholders of the corporation may determine the mode in which its property shall be disposed of, provided they act in good faith and in the interest of all the stockholders and creditors, and provided they are not controlled by express statutory provisions. Corporations, including railroad companies, if they are not excepted from the operation of the statute, have the power, at any time within the period for which their existence is extended, to convey their lands or other property to a trustee in trust to wind up their business.<sup>392</sup>

In disposing of the property of a corporation after expiration of its charter, under a statute continuing the existence of the corporation for the purpose of winding up its affairs, the property must be disposed of in the interest of all the stockholders. The power of the majority is not absolute. Neither the directors nor a majority of the stockholders can sell the property to a new corporation of which they are directors and stockholders, on an arbitrary estimate of its value made by themselves, and compel a dissenting minority of the stockholders, either to take shares in the new corporation in return for

Sage, 58 Fed. 651 (under the Min-391 State v. Fogerty, 105 Iowa, nesota statute). 32.

<sup>300</sup> Saltmarsh v. Planters' & Merchants' Bank, 14 Ala. 668.

<sup>892</sup> Hanan v. Sage, 58 Fed. 651

their shares in the old corporation, or to accept payment of their proportion in money on the basis of the estimated valuation. To allow this, it was said by the court in such a case, would result in compelling the minority to go into the new company, however much they may be convinced that it is not likely to be successful, or whatever other objections they may have to becoming members of that corporation, or else to receive, for the property which they have in the old corporation, a sum which is fixed by those who are buying them out.393

- (f) Liability for torts.—In West Virginia, where a statute provided in effect that when a corporation should expire or be dissolved suits might be brought, continued, or defended, property conveyed, and all lawful acts be done in the corporate name in the like manner and with like effect as before such dissolution or expiration, so far as necessary to wind up its affairs, it was held that a corporation continuing in business and committing a tort after the expiration of the term of its existence, as provided by its charter, was precluded from setting up the expiration of its corporate existence in an action against it for the tort.394
- (g) Actions and proceedings.—When, by a charter or general statutory provision, the existence of a corporation is continued after expiration or annulment of its charter, for the purpose of allowing it to prosecute and defend suits and wind up its affairs, any necessary action or other proceeding may be commenced by or against the corporation in the corporate name during the period for which its existence is thus continued.395

(under the Minnesota statute). See, also, Folger v. Chase, 18 Pick. (Mass.) 63.

393 Mason v. Pewabic Mining Co., 133 U.S. 50.

394 Miller v. Newburg Orrel Coal Co., 31 W. Va. 836, 2 Keener's Cas. 1929.

2 Ohio St. 167, 12 Ohio St. 577; Warner v. Callender, 20 Ohio St. 190; Richmond Union Passenger Ry. Co. v. New York & Sea Beach Ry. Co., 95 Va. 386; Wehn v. Fall, 55 Neb. 547; Blake v. Portsmouth & Concord Railroad, 39 N. H. 435; Bank of United States v. Leathers, 8 B. Mon. (Ky.) 126; Bewick v. 395 Tuskaloosa Scientific & Art Alpena Harbor Imp. Co., 39 Mich. Ass'n v. Green, 48 Ala. 346; Pom- 700; Crawford v. Planters' & Mereroy's Lessee v. Indiana Bank, 1 chants' Bank of Mobile, 6 Ala. 289; Wall. (U. S.) 23. See, also, Stet-State v. Bank of Washington, 18 son v. City Bank of New Orleans, Ark. 554; Campbell v. Mississippi And suits by or against the corporation pending at the time of the expiration or annulment of its charter do not abate. 396 Where the charter of a corporation declared that its powers should cease on a certain date, but that it should have all "necessary and incidental powers to collect and close up its business," it was held that an action against the corporation did not abate on the expiration of its charter, but might be prosecuted to final determination as unfinished business.397

In some states it is held that, where a statute continues the existence of a corporation for a certain period after its dissolution for the purpose of prosecuting and defending suits, etc., it becomes absolutely defunct upon the expiration of such period. in the absence of provision to the contrary, that no action can afterwards be brought by or against it, and that actions then pending by or against it abate. 398 In other states the construc-

Union Bank, 6 How. (Miss.) 625; years. Blake v. Portsmouth St. Louis & Sandoval Coal & Min- Concord Railroad, 39 N. H. 435. ing Co. v. Sandoval Coal & Mining Co., 111 Ill. 32; Boyd v. Hankinson (C. C. A.) Fed. 49; Schmidt & Bros. Co. v. Mahoney, 60 Neb. 20.

A statute continuing the charter of a corporation for the purpose of maintaining suits applies as well to suits commenced before its passage as to those instituted afterwards. Crawford v. Planters' & Merchants' Bank of Mobile, 6

Ala. 289.

In a statute providing that "any corporation whose powers may expire by express limitation, or otherwise, on any day, may continue to be a body corporate \* \* \* for the purpose of prosecuting and defending suits," etc., "the word 'may' is to be construed 'must' or 'shall,' where the public interest and rights are concerned, and the public or third persons have a claim de jure that the power shall be exercised," and the dissolution of a corporation by expiration of its charter or otherwise cannot prevent it from suing or being continuing the existence of every sued at any time within the three corporation whose charter

Where a statute provides for the application and distribution of the property of corporations on dissolution, and for continuance of the corporation for the purpose of suits, etc., the statute of limita-tions does not cease to run in favor of a corporation against an ordinary action at law to recover a judgment against it when the corporation is dissolved, and its property distributed. Bradley Salt Co. v. Norfolk Importing & Exporting Co. of Virginia (C. C. A.) 101 Fed. 681.

396 Foster v. Essex Bank, 16 Mass. 245, 8 Am. Dec. 135, 2 Smith's Cas. 608, 1 Cum. Cas. 464; Pomeroy's Lessee v. Indiana Bank, 1 Wall. (U. S.) 23; Bewick v. Al-pena Harbor Imp. Co., 39 Mich. 700; Cooper v. Oriental Savings & Loan Ass'n, 100 Pa. St. 402.

Bank, 1 Wall. (U.S.) 23,

398 Dundee Mortgage & Trust Inv. Co. v. Hughes, 77 Fed. 855.

Under a Massachusetts statute

tion of the statute is otherwise. 399 In any event, this can only apply where the circumstances are such as to bring the corporation within the provisions of the statute.400

the term of three years afterwards, for the purpose of prosecuting and defending suits by or against it, and enabling it gradually to settle and close its concerns, to dispose of and convey its property, and to divide its capital stock, and providing also for the appointment of a receiver, at any time within such three years, to do all acts which might have been done by the corporation if in being, for the final settlement of its unfinished busi-ness, it was held that a judgment recovered against a corporation after the expiration of three years from the repeal of its charter, without any receiver having been appointed, was void. Thornton v. Margin ' Freight Ry. Co., 123 Mass. 32, 1 Cum. Cas. 482.

399 In Franklin Bank v. Cooper, 36 Me. 179, it was held that where a statute provides that actions may be commenced in the name of a corporation for the benefit of its stockholders within limited  $\mathbf{a}$ time after the expiration of its charter, the power to commence actions within such time gives the power to prosecute them to final judgment after the expiration of such time. Franklin Bank Cooper, 36 Me. 179. See, also, Bewick v. Alpena Harbor Imp. Co., 39 Mich. 700.

Under a statute of Michigan providing that all corporations whose charters expire shall continue to be bodies corporate for three years for the purpose of prosecuting and defending suits by or against them, and that any suit pending in favor of a corporation at the time of its dissolution shall not abate, but may be prosecuted by the trustees on whom its estate shall have devolved, in its or their name, under the direction of the court in which the suit is pending, it was held by the Massachusetts court Hutchinson, 176 Ill. 48. that, where a Michigan corpora-

been annulled or has expired, for tion, shortly before the end of the three years next after the expiration of its charter, sold and assigned all its property and claims to an individual, upon his giving bond to pay its debts and do certain other things, the assignee could, after the expiration of the three years, prosecute to judgment, in the name of the corporation, a suit commenced in Massachusetts before the charter of the expired. Michigan corporation State Bank v. Gardner, 15 Gray (Mass.) 362.

> In Illinois, the statute (Rev. St. c. 32) provides (section 10) that certain corporations whose charters may have expired shall continue in their corporate capacity for two years for the sole purpose of collecting debts due, and selling and conveying their property: (section 11) that the corporate name may be used for such purpose, and that they shall be capable of prosecuting and defending all suits at law or in equity; and (section 12) that the dissolution for any cause whatever of any such corporation shall.not take away or impair any remedy given against such corporation, its stockholders or officers, for any liabilities incurred previous to its dissolution. Under these provisions it was held that a corporation sued for a debt incurred previous to the expiration of its charter may sue out a writ of error more than two years after expiration of its charter, notwithstanding the suing out of a writ of error is the beginning of a new suit, since section 12, supra, gives such creditors the right to sue, without any limitation as to time except that of the general statute of limitations, and since the practice act provides that a party to an action may prosecute a writ of error. Singer & Talcott Stone Co. v.

400 A statute providing that cor-

(h) Effect of statute on equity jurisdiction.—A statute continuing the existence of corporations after expiration or annulment of their charter for the purpose of allowing them to sue and be sued, and to wind up their affairs, does not take away the independently existing jurisdiction of a court of equity to administer the assets of a dissolved corporation for the benefit of those who are entitled thereto.401

#### § 333. Officers as trustees for creditors and stockholders.

- (a) In general.—In some states it is provided by statute that, on the dissolution of a corporation, its directors or other officers shall be trustees for the creditors and stockholders, with power to settle the affairs of the corporation, collect the outstanding debts, and divide the money and other property among the stockholders after paying the corporate debts. 402 Such a statute does not take effect until actual dissolution. As was shown in a previous section, insolvency does not dissolve a corporation. 403 A corporation, therefore, which, though insolvent, continues to hold meetings and transact business, and against which a suit is pending and judgment rendered, is not within the operation of a statute providing that, on dissolution of a corporation, the president and directors or managers shall be trustees to settle its affairs. 404 Such a statute takes effect on dissolution of a corporation, ipso facto, by reason of failure to comply with a condition subsequent in its charter.405
  - (b) Who are "creditors."—The New York statute and the

porations whose charters have "expired or been annulled" shall continue as bodies corporate for three years for the purpose of winding up their business, etc., does not apply where a corpora-tion's charter has neither expired nor been annulled, but it has merely closed up its business and settled with its members, and the expiration of three years after such settlement does not prevent a suit against it. Heggie v. People's Building & Loan Ass'n, 107 N. C. 581.

401 State v. Bank of Tennessee,

5 Baxt. (Tenn.) 101. See, also, School District No. 3 v. Town of Greenfield, 64 N. H. 84.

\*\*\* See Adams v. Kehlor Milling Co., 35 Fed. 433; Clark v. City & County of San Francisco, 53 Cal. 306; Havemeyer v. Superior Court, 84 Cal. 327, 18 Am. St. Rep. 192. 403 Ante, § 311.

404 Adams v. Kehlor Milling Co.,

35 Fed. 433.

405 Ford v. Kansas City & Independence Short Line R. Co., 52 Mo. App. 439; ante, § 306.

statutes in several other states make the directors or trustees of a dissolved corporation trustees for its "creditors" and stockholders, and the question has arisen, who are creditors within the meaning of the statute? The term clearly applies to persons to whom the corporation is indebted by reason of a contract or a judgment, but whether the term "creditors" includes persons having a claim against a corporation for damages for a tort is not so clear. In New York, after some difference of opinion among the judges of the supreme court, it was held that such persons were within the statute, and that the trustees might be sued by a person having a claim against the corporation for loss of the services of his son, who was injured by reason of negligence of the corporation while he was in its employ-The term "creditors," it was said, includes all those to whom the corporation was under any enforceable obligation, as well as those to whom it was indebted. 406

(c) Property rights.—Under a statute making the directors or other officers of a corporation, on its dissolution, trustees for creditors and stockholders for the purpose of settling its affairs, the property rights of a corporation survive its dissolu-Thus it has been held, under such a statute, that on the forfeiture of the charter of a railroad company for failure to comply with conditions subsequent as to the construction, equipment, and operation of its road, its property rights survive for

398.

In Hepworth v. Union Ferry Co., court it was held that a person 62 Hun (N. Y.) 257, it was held, having a claim for damages under such a statute, that a per- against a corporation for such son who had a claim for damages torts or for personal injuries was against a corporation, for an as-sault committed by its servant, or ing of the statute, and that the for death by wrongful act, was a right of action therefor did not creditor within the meaning of the survive dissolution of the corporastatute, and that an action against tion. Grafton v. Union Ferry Co.,

406 Marstaller v. Mills, 143 N. Y. sion in People v. Troy Steel & Iron Co., 82 Hun (N. Y.) 303.

In other cases in the supreme the corporation therefor pending 22 Civ. Proc. R. (N. Y.) 402, af-when its charter expired could be firming 20 Civ. Proc. R. 238; In continued against the directors as re New York Oxygen Co., 24 Civ. trustees. There was a like deci- Proc. R. (N. Y.) 398. the benefit of its creditors and stockholders.407 The same, of course, is true of other corporations. 408

Under the New York statute providing that, on the dissolution of any corporation, the directors or managers at the time of its dissolution shall be the trustees of the creditors and stockholders, with full power to settle and wind up the affairs of the corporation, it has been held that, immediately upon the dissolution of a corporation, the directors or trustees become vested with the title to the corporate property.409

(d) Actions and parties.—The question as to who is the proper party to sue and be sued under statutes making the directors, trustees, or other officers of a dissolved corporation trustees for creditors and stockholders, and giving them power to settle and wind up the affairs of the corporation, depends upon the terms of the particular statute. In some jurisdictions, actions may be brought in the name of the corporation, 410 while in others they are brought by or against the trustees.411 A statute merely constituting the directors of a corporation trustees for creditors and stockholders on its dissolution does not continue the ex-

Canal & Milling Co., 12 Colo. 230, it was held that, under a statute empowering a corporation to convey its property, and a statute by which its property, on its dissolu-tion, passes to its directors in trust, instead of reverting, the right of way of a ditch company, which has been conveyed by it, does not cease on the expiration of its charter, but continues in the grantee.

400 People v. O'Brien, 111 N. Y. 1, 7 Am. St. Rep. 684, 2 Smith's Cas. 728.

410 Saltmarsh v. Planters' & Mer-

407 Sulphur Springs & Mt. Pleas- Marstaller v. Mills, 143 N. Y. 398; ant Ry. Co. v. St. Louis, Arkansas Sturges v. Vanderbilt, 73 N. Y. & T. Ry. Co., 2 Tex. Civ. App. 650. 384; Consolidated Association of T. Ry. Co., 2 Tex. Civ. App. 650. 384; Consolidated Association of the In Balley v. Platte & Denver the Planters of Louisiana v. Mason, 24 La. Ann. 518.

Under a statute providing that in certain cases, on the dissolu-tion of a corporation, the directors at the time of dissolution and the survivors of them should be trustees for creditors and stockholders, and authorizing them as such to sue "by the name of the trustees of such corporation, describing it by its corporate name," it was held that it authorized persons so constituted trustees of a dissolved corporation to sue under their collective title, "trustees of" chants Bank, 14 Ala. 668; Crews v. Farmers' Bank of Virginia, 31 Grat. (Va.) 348.

411 Martin v. Belmont Bank of St. Clairsville, 13 Ohio, 250; Paola Town Co. v. Krutz, 22 Kan. 725; Ohio, 250. istence of the corporation, so as to render it capable of suing or being sued in the corporate name after expiration of its charter. 412

- (e) Liability of officers as trustees.—Where a statute makes the president and directors trustees of a dissolved corporation, they are jointly and severally responsible for the misappropriation of assets. If they conduct the business of the corporation after expiration of its charter, without attempting to wind it up, they may be made to account in proceedings by stockholders to wind up the affairs of the corporation. 414
- —Distribution among stockholders.—Officers of a corporation intrusted with the distribution of its funds among the stockholders are not liable for giving a portion of the stockholders more than their share, where they acted in good faith, and pursuant to a plan of distribution adopted by a majority of the stockholders.<sup>415</sup>

In distributing the assets of a joint-stock corporation among the stockholders on its dissolution, as in the payment of dividends, 416 it is not necessary that the officers shall require persons claiming to be stockholders to produce their certificates of stock, but they may safely make the distribution to those who appear as stockholders on the stock books of the corporation, for, when a corporation is merely performing a corporate duty with respect to stockholders, its own record is all it need consult. "As between adverse claimants of the certificate," said the Pennsylvania court in such a case, "the possession of it with the transfer upon it is often the test of the title. But when the corporation itself is not dealing with its stockholder on the security of his stock, and is merely performing a corporate duty, its own record is all it needs to consult, for whoever would

<sup>412</sup> Sturges v. Vanderbilt, 73 N. Y. 384.

<sup>414</sup> Mason v. Pewabic Mining Co., 133 U. S. 50.

<sup>413</sup> Sprague-Brimmer Mfg. Co. v. M. J. Murphy Furnishing Goods Co., 26 Fed. 572.

<sup>415</sup> Goodrich v. City Loan & Building Ass'n, 54 Ga. 98.

<sup>416</sup> Post, chapter xxii.

demand the privileges of a stockholder should produce the evidence of his fitle and ask to be permitted to participate."417

#### § 334. Appointment of receiver or trustee.

(a) In general.—In many states there are statutes providing for the appointment by a court of a receiver or trustee to take charge of and collect the assets of a corporation after it has been dissolved, and wind up its business.418 And sometimes provision is made for the appointment of a receiver pending proceedings to dissolve a corporation.419

To give a court jurisdiction under a statute to appoint a receiver of a corporation after its dissolution, or pending proceedings for its dissolution, or to appoint a successor in case of the death of a receiver, the particular court must be authorized by the statute to make the appointment. 420 And the circumstances must be such as to bring the case within the statute. 421

73 Pa. St. 59, 64.

418 See Hale-Berry Co. v. Diaing Co.,111 Ill. 32; People v. Northern R. Co., 53 Barb. (N. Y.) 98.

dissolution of a corporation, a receiver may be appointed pendente lite before service on the corpora-tion. St. Louis & Sandoval Coal the appointment of a receiver for & Mining Co. v. Sandoval Coal & a reporation by the court in which Mining Co., 111 Ill. 32.

In an action by the trustees and stockholders of a corporation to dissolve the corporation because cessor in case of the death or a of insolvency, a receiver may be appointed under a statute provid-clusive, and the supreme court, to ing that a receiver may be appointed by the court in which an has no jurisdiction to make the action is pending or has passed appointment. State v. Orleans Navigation Co., 9 La. Ann. 40.

\*\*Proper v. Superior Court, 108 tion has been dissolved or is insolvent, or in imminent danger of insolvency. Security Savings & Cal. 431; Havemeyer v. Superior Court, 84 Cal. 327, 18 Am. St. Rep. Trust Co. v. Piper (Idaho, 1895) 192. 40 Pac. 144.

417 Appeal of Bank of Commerce, poration asking to be dissolved, under a statute providing for the appointment of a receiver by the mond State Iron Co., 94 Ga. 61; court in which an action is pend-St. Louis & Sandoval Coal & Mining, or under a statute providing ing Co. v. Sandoval Coal & Minthat, when suits may be brought against stockholders, courts of equity shall have full power to 419 In Illinois, in a suit for the dissolve the corporation and appoint a receiver. Jones v. Bank of Leadville, 10 Colo. 464.

a proceeding for its dissolution is pending, the implied jurisdiction of that court to appoint a suc-cessor in case of the death of a

Under the provision of the code The court has no authority to of California that a receiver may appoint a receiver on an ex parte be appointed "in cases where a application by an insolvent cor- corporation has been dissolved, or

A statute providing that a court which has rendered judgment of ouster may appoint a receiver for a corporation previously dissolved, "the affairs of which have not been settled and adjusted," does not authorize appointment of a receiver where the corporation, before the commencement of the proceedings in quo warranto, has made an assignment, and the assignee has entered upon his duties under the direction of a court of competent jurisdiction.422

Under a statute authorizing the court to appoint a receiver upon the "dissolution" of a corporation, the power to appoint a receiver does not exist unless a corporation is dissolved. Therefore, there is no power to appoint a receiver after a judgment, in an action by the attorney general under a statute, merely ousting a corporation from usurping certain privileges and franchises not conferred upon it by its charter, for such a judgment does not dissolve the corporation. 423

Even in the absence of a statute, a court of equity, as was shown in a previous section, has authority to appoint a receiver, after a corporation has been dissolved, to take charge of, collect, and administer its assets; 424 and when a court of equity has jurisdiction to dissolve a corporation and wind up its affairs in a suit by stockholders, it has jurisdiction to appoint a receiver pending the suit, if necessary to preserve the assets of the corporation and protect the rights of creditors and stock-When a corporation ceases to act, and the president

its corporate rights," a court which 101 Cal. 135. renders a judgment of forfeiture of the state for abuse of its franchises has no authority to appoint a receiver of the corporate assets, unless at the instance of some person interested as a creditor or stockholder, and upon a showing that such appointment is necessary for the protection of their Havemeyer v. Superior Court, 84 Cal. 327, 18 Am. St. Rep. 192. See, also, Harrison v. Heb- (N.Y.) 166. See post, chapter xxiv.

is insolvent, or in imminent dan- bard, 101 Cal. 152; State Investger of insolvency, or has forfeited ment & Ins. Co. v. Superior Court.

In Indiana, the court may apagainst a corporation at the suit point a receiver in proceedings by the state to forfeit the charter of a corporation. Eel River R. Co. v. State, 155 Ind. 433.

> 422 Com. v. Order of Vesta, 156 Pa, St. 531.

> 428 Yore v. Superior Court, 108 Cal. 431.

424 Ante, § 328(b).

425 Conro v. Gray, 4 How. Pr.

and principal stockholders assume to use the property as their own, creditors are entitled to come into a court of equity and ask for and obtain the appointment of a receiver. 426

It has been held in Pennsylvania that, in the absence of a statutory provision therefor, the court has no power to appoint a receiver for a corporation on motion of the state or commonwealth in quo warranto proceedings to forfeit its charter.427 But in a New York case it was held that when the charter of a corporation is forfeited in proceedings under a statute because of its suspension of business for a certain period, the judgment may properly include the appointment of a receiver. 428

The mere fact that a corporation has been dissolved does not necessarily give the minority stockholders the right to have a receiver appointed, and the assets sold. They have no such right if the circumstances are such as to justify a court of equity in ascertaining the value of the assets without a sale, and in making a distribution to the members on that basis. 429

- (b) Appointment of successor.—When a court is given jurisdiction to appoint a receiver for a dissolved corporation, it has the implied power to appoint a successor in case of the death or removal of its appointee.430
- (c) Appointment by governor or legislature.—In some jurisdictions there have been statutes authorizing the governor toappoint a receiver or liquidator to take charge of and liquidate the affairs of a corporation, when its charter has expired or been annulled, and there is no law existing at the time which provides for its liquidation. Such a statute applies where special acts in relation to the liquidation of the affairs of corporations

<sup>426</sup> Conro v. Gray, 4 How. Pr. a receiver, or to take an account. (N. Y.) 166.

<sup>427</sup> Com. v. Order of Vesta, 156 Pa. St. 531.

As no original equity jurisdiction was conferred by the consti-tution of Wisconsin upon the su-preme court, except to issue an injunction, it was held that it had no power, upon rendering a judgment of forfeiture and dissolution against a corporation, to appoint tion Co., 9 La. Ann. 40.

and make a distribution among creditors and stockholders. v. West Wisconsin Ry. Co., 34 Wis. 197.

<sup>428</sup> People v. Northern R. Co.,. 53 Barb. (N. Y.) 98.

<sup>429</sup> Baltimore & Ohio R. Co. v. Cannon, 72 Md. 493.

<sup>430</sup> See State v. Orleans Naviga-

have expired by limitation prior to the appointment by the governor. 431

When a corporation is dissolved by an act of the legislature repealing its charter, the repealing act may appoint a suitable person to collect and distribute the assets of the corporation.<sup>432</sup>

(d) Where a trustee or receiver has been appointed by or with the consent of the corporation.—A receiver will not necessarily be appointed after or pending the dissolution of a corporation, where persons appointed by the officers or stockholders are in charge of the affairs of the corporation. Where persons in charge of the property and affairs of a corporation as liquidators of the same pending its dissolution were elected as such by the stockholders, and their election had not been set aside, and no fear of fraudulent action on their part was alleged, it was held that they should not be dismissed by the court, and a receiver appointed in their stead.<sup>433</sup>

Where the charter of a corporation vested the liquidation of its affairs in the stockholders through commissioners appointed by them, and the stockholders consented to the appointment of a receiver by the court, at the suit of creditors praying therefor, it was held that the appointment would not be disturbed on appeal of creditors.<sup>434</sup>

When the charter of a corporation is declared forfeited in proceedings by the state, it is discretionary with the court to leave the liquidation of its affairs in the hands of the liquidators appointed by the corporation before the institution of the proceedings, where the corporation is not indebted, and the stockholders do not object.<sup>435</sup>

(e) Where the directors or other officers are made trustees.— The fact that there is a statute making the directors, trustees, or other officers of a dissolved corporation trustees for the cred-

<sup>431</sup> State v. Haynes, 12 La. Ann. 434 In re Louisiana Savings Bank 285. & Safe Deposit Co., 35 La. Ann. 432 Western North Carolina R. 196. Co. v. Rollins, 82 N. C. 523.

<sup>433</sup> Follett v. Field, 30 La. Ann. 435 State v. Herdic Coach Co., 161. 35 La. Ann. 245.

itors and stockholders, with power to wind up and settle its affairs, etc., does not necessarily destroy the jurisdiction of courts of equity to appoint a receiver. Such jurisdiction exists, notwithstanding the statute, when the appointment of a receiver is necessary for the protection of creditors or stockholders, as where the directors or other officers are guilty of fraud or unreasonable delay in the execution of the trust.<sup>436</sup> But a receiver should not be appointed if the directors or other officers are properly winding up the affairs of the corporation, and are in all respects trustworthy.<sup>437</sup>

Notwithstanding a general law providing that, upon the dissolution of a corporation, the directors shall be trustees for creditors and stockholders, with power to hold the property and rights of the corporation, the legislature, upon dissolving a corporation, may appoint other trustees.<sup>438</sup>

In California, a section of the Code in relation to the dissolution of corporations provides that the directors or managers of a corporation at the time of its dissolution shall have the power to settle its affairs, unless third persons are appointed by the court, and another section declares that, on the dissolution of a corporation, the superior court may appoint one or more persons receivers or trustees, on the application of a creditor or stockholder. Under these provisions, it has been held that, where the charter of a corporation has been forfeited by the state, an application for a receiver to settle up its affairs cannot be sustained on the ground that it will defeat the forfeiture to allow its directors to retain control of its assets; <sup>439</sup> and that these statutes do not authorize the court to appoint a receiver on dissolution of a corporation in an action by the attorney general. <sup>440</sup>

(f) Where existence of corporation is continued by statute.— In those states in which there is a statute continuing the ex-

<sup>436</sup> In re Pontius, 26 Hun (N. Y.)

<sup>&</sup>lt;sup>437</sup> City Pottery Co. v. Yates, 37 N. J. Eq. 543. And see Havemeyer v. Superior Court, 84 Cal. 327, 18 Am. St. Rep. 192; Anderson v. Buckley (Ala.) 28 South. 729.

<sup>438</sup> McLaren v. Pennington, 1, Paige (N. Y.) 102.

<sup>439</sup> Havemeyer v. Superior Court, 84 Cal. 327, 18 Am. St. Rep. 192.

 <sup>440</sup> State Investment & Ins. Co.
 v. Superior Court, 101 Cal. 135.

istence of corporations whose powers have expired by limitation, forfeiture, or otherwise, for the purpose of allowing them to wind up their affairs, the court may appoint a receiver under some circumstances. In a North Carolina case it was held that the statute of that state continuing the existence of defunct corporations for three years after expiration of their charters, for the purpose of bringing and defending suits, and closing up their business, ousts the former equity jurisdiction to appoint a receiver of a corporation, at the instance of creditors, to wind up its affairs.

But in Illinois, where the statute relating to corporations provides that corporations organized under it, whose powers have expired by limitation or otherwise, shall continue their corporate capacity, with the use of their names, for two years, for the purpose of settling their affairs, conveying property, and prosecuting and defending suits, and that dissolution for any cause whatever shall not impair any remedies against it, or its officers or stockholders, for liabilities incurred before dissolution, it has been held that, upon judgment of ouster in quo warranto proceedings, the corporation becomes a trustee for creditors and stockholders, and that equity will have jurisdiction, on the ground of the trust relation, of a suit by a stockholder, in behalf of himself and other stockholders who may join with him, to appoint a receiver to administer its assets, where it appears that the affairs of the corporation are involved, and its property in danger of being seized and dissipated by means of attachments, executions, etc.443

(g) Time of application or appointment.—The proper time for appointment of a receiver under a statute depends, of course, upon the provisions of the particular statute. A premature appointment is void, or at least subject to be set aside. Thus, under a statute providing that, on the presentation of a petition

<sup>441</sup> See ante, § 332.
443 Olmstead v. Distilling & Cat442 Von Glahn v. De Rosset, 81 tle Feeding Co., 73 Fed. 44.
N. C. 467.

for the voluntary dissolution of a corporation, an order shall be made requiring all persons interested to show cause before a referee, appointed to take proofs and report to the clerk, why a decree of dissolution should not be granted, and, on the coming in of the referee's report, the court shall determine whether or not to dissolve the corporation, it is error to appoint a receiver for the corporation on presentation of a petition by its trustees for its dissolution, or on the resolution of the order to show cause 444

The appointment of a receiver, after a judgment forfeiting the charter of a corporation for misuser or abuse of its franchises, to sell the property of the corporation and wind up its affairs, is a proceeding upon the judgment within the meaning of a statute providing that an appeal "stays all proceedings upon the judgment or order appealed from, or upon the matters embraced therein," and such an appointment, therefore, pending an appeal from the judgment, is void.445

In proceedings by the attorney general in the nature of quo warranto to dissolve a corporation, the court has no power to appoint a receiver before judgment, except in the case of insolvency.446

It is also necessary, where a statute authorizes the appointment of a receiver of a corporation within a certain time after its dissolution, on the application of a creditor or stockholder, that the appointment, or at least the application, shall be made within the time limited.447

444 Chamberlain v. Rochester 446 People v. Washington Ice Co., Seamless Paper Vessel Co., 7 Hun 18 Abb. Pr. (N. Y.) 382. (N. Y.) 557.

York statute for the voluntary dissolution of a corporation, it was held that a receiver could not be Hun (N. Y.) 369.

445 Havemeyer v. Superior Court, 84 Cal. 327, 18 Am. St. Rep. 192; State Investment & Ins. Co. v. Superior Court, 101 Cal. 135.

447 Where a statute authorized In proceedings under a New the court, on the application of any creditor or stockholder, to appoint a receiver for a corporation on the expiration of its charter, or within appointed before the entry of a the three years thereafter allowed final order of dissolution. In re by statute for winding up its af-E. M. Boynton Saw & File Co., 34 fairs, it was held, in an action by a person as receiver of a corporation on a note, that an answer alleging that the charter of the corporation expired on a certain day, that no receiver was appoint-

A statute authorizing the court, on the application of any creditor or stockholder, to appoint a receiver for a corporation on the expiration of its charter, or within the three years thereafter allowed by statute for winding up its affairs, does not require that the receiver shall be actually appointed within the three years, but, if the application is made within that time, the court may act upon it afterwards.448

- (h) Who may apply for a receiver.—The persons who may apply for a receiver will depend upon the particular statute under which his appointment is authorized. Generally the statutes allow the application to be made by any creditor or stockholder. Unless it is otherwise provided by statute, the state, if it is not interested, cannot apply for the appointment of a receiver for a corporation after its charter has been forfeited.449
  - (i) Who may be appointed receiver.—Generally the statutes authorizing the appointment of a receiver do not require the appointment of any particular person, and the court may appoint any suitable person. A creditor, stockholder, or officer of the corporation may be appointed. 450 In the absence of provision to the contrary, another corporation may be appointed to act as receiver, if the powers conferred upon it by its charter are such as to permit it to act in such a capacity.451
  - (i) Order appointing receiver.—The order of the court appointing a receiver must comply with the requirements of the

ed during the three years follow- full power to settle its affairs, and

449 In California, where the code unless third persons are appointed by the court, the directors or N. W. 1004. managers of a corporation at the time of its dissolution shall have Co. v. Rollins, 82 N. C. 523.

ing, and that no application for a provides in a subsequent section time, was not demurrable. Hatfield v. Cummings, 140 Ind. 547. appoint one or more persons reSee, also, Bigelow v. Union Freight
R. Co., 137 Mass. 478. receiver was made during that that on the dissolution of a cor-448 Lime City Building, Loan & it was held that where the char-Savings Ass'n v. Black, 136 Ind. ter of a corporation had been for-544; Hatfield v. Cummings, 140 feited, the state had no such interest in its affairs as to entitle it to apply for a receiver. Haveprovides for the dissolution of meyer v. Superior Court, 84 Cal. corporations, and declares that, 327, 18 Am. St. Rep. 192.

450 Moran v. Hosmer (Mich.) 83

451 Western North Carolina R.

statute under which the appointment is made, but defects therein, if they are such as may be cured by an amendment nunc pro tunc, will not render the appointment void. It was so held in a New York case where, in proceedings for the voluntary dissolution of a corporation, the order appointing a receiver, and to show cause why the corporation should not be dissolved, failed to require its publication, as required by the statute.<sup>452</sup>

(k) Effect of appointment of receiver.—Generally, when a permanent receiver is appointed for a corporation under a statute pending proceedings to wind up the affairs of the corporation, or after dissolution, the right of the corporation to prosecute an action previously commenced by it is suspended. The right of action vests in the receiver, and he may, under the direction of the court appointing him, continue or dismiss the action, as may be deemed best for the interests of the trust estate.<sup>453</sup>

After a judgment dissolving a corporation and appointing a receiver, an action cannot be commenced against it by service of process on an officer, or otherwise. Unless the statute provides otherwise, appointment of a receiver pending proceedings for the dissolution of a corporation, there having been no decree of dissolution, does not prevent an action against the corporation for a breach of contract or other cause of action which accrued before the appointment of the receiver.

(1) Transfer of property.—The statutes sometimes provide that a transfer of property of a corporation after the commencement of proceedings to dissolve the corporation shall be void as against the receiver appointed in such proceedings. A judgment by default against a corporation for a just debt is not within such a provision.<sup>456</sup>

<sup>452</sup> In re Christian Jensen Co., 128 N. Y. 550, affirming 59 N. Y. Super. Ct. 552.

<sup>468</sup> Kokomo City Street R. Co. v. Pittsburg, Cincinnati, Chicago & St. L. Ry. Co. (Ind. App.) 58 N. E. 211.

<sup>454</sup> Hetzel v. Tannehill Silver Mining Co., 4 Abb. N. C. (N. Y.) 40; Tinkham v. Borst, 15 How. Pr. (N. Y.) 204.

<sup>455</sup> Fleischauer v. Dittenhoefer, 49 N. Y. Super. Ct. 311. 456 In re Muehlfeld & Haynes

(m) Powers and duties of receivers.—A receiver of a corporation appointed by a court under statutory authority is generally invested by the statute with full title to the property and choses in action of the corporation, 457 in whatever jurisdiction the same may be situated, 458 and is the proper party to suits in relation thereto.459 And he may make sales and conveyances of property, with the approval of the court, in order to realize funds for the payment of debts, or for distribution among the stockholders.460

A receiver, however, even when the statute under which he is appointed expressly vests in him all the property and effects of the corporation, takes, as under any other assignment by operation of law, such property and effects only as the corporation held or was possessed of or entitled to for its own benefit.461 For example, he does not take property held by the corporation in trust, as a fund lawfully set apart and actually appropriated by the corporation out of surplus profits for

457 American Nat. Bank of Denver v. National Benefit & Casualty Co., 70 Fed. 420; Commercial Bank of Natchez v. Chambers, 8 Smedes & M. (Miss.) 9; Tinkham v. Borst, 15 How. Pr. (N. Y.) 204.
But where a receiver was ap-

pointed for a corporation under an act providing for its dissolution, but no decree dissolving it was entered, it was held that the title of the receiver to the property of the corporation remained inchoate. and the legal title to land previously conveyed to the corporation did not vest in the receiver by virtue of his appointment. Mont-gomery v. Merrill, 18 Mich. 338.

458 American Nat. Bank of Denver v. National Benefit & Casualty Co., 70 Fed. 420.

459 See cases above cited. And see Hetzel v. Tannehill Silver Mining Co., 4 Abb. N. C. (N. Y.) 40; Tinkham v. Borst, 15 How. Pr. (N. Tinkham v. Borst, 15 How. Pr. (N. 461 Le Roy v. Globe Ins. Co., 2 Y.) 204; Kokomo City Street R. Edw. Ch. (N. Y.) 657, 1 Smith's Co. v. Pittsburg, Cincinnati, Chi- Cas. 325.

Piano Co., 12 App. Div. (N. Y.) cago & St. L. Ry. Co. (Ind. App.) 58 N. E. 211.

> As to the appointment of a temporary receiver, see infra (n).

> 460 Where a receiver has been appointed pendente lite in a suit to dissolve a corporation, before service upon the corporation, he has no authority to sell the property of the corporation before service upon it. St. Louis & Sandoval Coal & Mining Co. v.. Sandoval Coal & Mining Co., 111 Ill.

> When a receiver of a corporation appointed in dissolution proceedings applies for confirmation of a sale of the property of the corporation subject to all legal liens, and the application is op-posed by creditors on the ground that a mortgage executed by the corporation is invalid, the receiver must show that the mortgage is a valid lien. In re Wendler Machine Co., 2 App. Div. (N. Y.) 16.

the payment of dividends declared by it.462 And he acquires no title whatever to property or choses in action validly conveyed or assigned by the corporation before his appointment, and before the dissolution of the corporation.463

The receiver or trustee of a dissolved corporation has authority to collect debts due the corporation.464 And for the purpose of collecting debts or enforcing other rights in favor of the corporation, he may bring any action which might be brought by the corporation if it were in existence. 465 in some states, sue for the benefit of creditors to enforce a statutory liability of the stockholders of the corporation.466 may sue the late directors or other officers of the corporation to recover damages for maladministration of its affairs. 467

Under a statute providing that, on dissolution of a corporation, a court may appoint a receiver to administer the assets of the corporation under its direction, a receiver thus appointed pending an action on behalf of the corporation brought by its treasurer is entitled to be made a party plaintiff to such And he may be substituted as a party defendant action.468 in a pending action against the corporation, if the motion to substitute is made in due time.469

462 Le Roy v. Globe Ins. Co., 2 Division No. 15, Sons of Temper-Edw. Ch. (N. Y.) 657, 1 Smith's ance, v. Aston, 92 N. C. 578. Cas. 325.

Smedes & M. (Miss.) 516.

464 A delinquent debtor of a corporation whose charter has been forfeited in quo warranto by the state, and for which a receiver or trustee has been appointed under a statute to collect assets and pay debts, cannot plead the judgment of forfeiture to defeat an action by the receiver or trustee. Lum v. Robertson, 6 Wall. (U. S.) 277. 465 French v. Landis, 12 Rob. (La.) 633.

Compare Fleischauer v. Ditten-463 See Bacon v. Cohea, 12 hoefer, 49 N. Y. Super. Ct. 311.

466 Herkimer County Bank v. Furman, 17 Barb. (N. Y.) 116; Walker v. Crain, 17 Barb. (N. Y.) 119. See post, chapter xxv.

467 French v. Landis, 12 Rob. (La.) 633.

468 Houston v. Redwine, 85 Ga.

469 When a receiver has been appointed on the dissolution of a corporation against which an action is pending, a motion to sub-A receiver appointed under a stitute him as a party defendant statute to settle the affairs of a in its stead comes too late after he corporation whose charter has ex- has distributed the assets, under pired may maintain actions on be- an order of the court, in satisfachalf of the corporation. Asheville tion of claims duly advertised for

Generally, actions by a receiver are brought in his name. but sometimes, by statute, they may be brought by him in the name of the corporation, 470 or either in his own name, or in the name of the corporation.471

(n) Temporary receiver.—In some states, the statute provides for the appointment of a temporary receiver in proceedings for the dissolution of a corporation.472 Appointment of a temporary receiver pending proceedings to dissolve a corporation under the New York statute does not divest the corporation of its title to property, or prevent it from suing and being sued, and it may sue, therefore, for an injury to its property before the appointment of a permanent receiver. 473 The corporation, notwithstanding the appointment of a temporary receiver, may move to vacate an attachment against its prop-Such appointment does not affect an action pending against the corporation, and a judgment duly entered therein is conclusive on the permanent receiver when appointed.475

the voluntary dissolution of a corporation as insolvent, under the New York statute, its directors v. Gardner, 124 N. Y. 334; Herhave filed a schedule under Code Civ. Proc. § 2421, showing at that time the assets and liabilities of the company, and it appears therefrom that the assets exceed the liabilities by a large sum, the appointment of a temporary receiver 473 Mutual Brewing Co. v. New York & College Point Ferry Co., 624 College Point Ferry

and proved under the statute. is unauthorized by section 2423, Owen v. Kellogg, 56 Hun (N. Y.) which allows such appointment where it has been made to appear "that the corporation is insolvent." In re Hitchcock Mfg. 471 Gray v. Lewis, 94 N. C. 392. Co., 1 App. Div. (N. Y.) 164. 472 Where, in an application for the voluntary dissolution of a corp.

#### CHAPTER XVIII.

## SUCCESSION OF CORPORATIONS; REORGANIZATION; CONSOLIDATION.

- I. Succession in General: Reorganization.
  - § 335. In general.
    - 336. Power to transfer property and franchises.
    - 337. Authority to reincorporate or reorganize.
    - 338. Transfer as a dissolution.
    - 339. Whether a new corporation is created, or an old corporation continued.
    - 340. Whether purchasers become a corporation.
    - 341. Property, rights, powers, franchises, and privileges of succeeding corporation.
    - 342. Liabilities of succeeding corporation.
    - 343. Liability of old corporation.
    - 344. Change of state or other bank to a national bank.
  - 345. Reorganization agreements, and rights or shareholders, bond-holders, and creditors generally.
  - 346. Promotion of reorganizations.

#### II. CONSOLIDATION OF CORPORATIONS.

- § 347. In general.
  - 348. What constitutes a consol idation.
  - 349. Power to consolidate.
  - 350. Mode of effecting consolidation.
  - 351. Effect of unauthorized or ineffectual consolidation.
  - 352. De facto corporate existence.
  - 353. Estoppel to deny validity of consolidation.
  - 354. Dissolution of consolidating corporations, and creation of new corporation.
  - 355. Rights, powers, franchises, privileges, and property of consolidated corporation.
  - 356. Burdens and liabilities of consolidated corporation.
  - 357. Rights of creditors against consolidating corporations.
  - 358. Effect of consolidation as to liens.
  - 359. Rights and liabilities of stockholders.
  - 360. Authority of officers.
  - 361. Effect of consolidation on pending actions and proceedings
  - 362. Consolidation of corporations of different states.
  - 363. Remedies in case of unauthorized or defective consolidation

#### I. SUCCESSION IN GENERAL; REORGANIZATION.

§ 335. In general.—Subject to the limitations imposed by the doctrine of ultra vires, and to the rights of stockholders and creditors, one corporation may succeed to the property and franchises of another corporation by a direct purchase and transfer, or by purchase of the same at a sale under execution, or under foreclosure of a mortgage, or other judicial sale. And in such a case difficult questions arise as to its rights and liabilities, and the rights and liabilities of its stockholders and creditors. These are explained in the following pages.

Reorganization of a corporation is where an existing corporation is organized anew. Whether the corporation is merely continued, or a new corporation created, depends upon the intention.

When a corporation succeeds to the property, franchises, and business of another corporation—

- (1) The property, rights, franchises, and privileges of the succeeding corporation depend upon the terms of the transfer, assuming it to be valid, and upon the statute by or under which the corporation is created, and the statute, if any, by or under which the transfer is made.
  - (2) The succeeding corporation is not liable for the debts or on the general contracts of the old corporation, or for its torts; nor is the property in its hands liable therefor—
    - (a) Unless there is an express agreement to pay or assume the same.
    - (b) Or unless there are circumstances from which such an agreement may be implied.
    - (c) Or unless the circumstances are such as to render the transfer a fraud upon the creditors of the old corporation.
    - (d) Or unless the corporation is a mere continuance of the old corporation.
    - (e) Or unless liability is imposed by statute.
    - (f) Or unless the liability arises out of an obligation or covenant running with the property acquired.

When a state bank is reorganized as a national bank, as permitted by act of congress, the national bank, as the successor of

the state bank, acquires all its assets and rights, and assumes all its liabilities. A new corporation is not created.

Succession in general.—The term "succession" with reference to corporations is used here broadly to designate any proceeding or transaction by which one corporation succeeds to or acquires the property, or property, franchises, and business of another corporation, or of a partnership or natural person, or by which a natural person succeeds to the property, or property, franchises, and business of a corporation.

Succession may take place in various ways. It may take place by virtue of a direct sale and transfer of its property, or property and franchises, by one corporation to another, by a natural person or partnership to a corporation, or by a corporation to a natural person or partnership. The succession by a corporation to the property and business of a partnership has been somewhat considered in a former section.<sup>1</sup>

A corporation may also succeed to the property, or property, franchises, and business of another corporation by purchasing the same at a sale on execution against it, or at a sale under a decree foreclosing a mortgage executed by it, or other judicial sale.<sup>2</sup>

The charter of a corporation may be amended, or extended, or even revived after its expiration, without affecting its existence or identity in any way. In such a case, of course, there is, strictly speaking, no succession at all. The corporation, before and after the amendment, extension, or revival, is the same body, both in fact and in law.<sup>3</sup>

Reincorporation.—If a new charter is granted by a special act to a body of men composing an existing corporation, and the old corporation is dissolved, there is a "reincorporation." And the same is true where an existing corporation is dissolved, with the consent of the state, and a new corporation formed under a general law. This term cannot properly be applied

<sup>1</sup> Ante, § 112. 3 See ante, § 57(g), 58; post, § 2 See post, § 342(b),(c),(d). 339(d-g), 342(j).

except where the old corporation is dissolved, and an entirely new and distinct corporation is created, but it has sometimes been applied, improperly, both by legislatures and by judges, to reorganization of corporations and amendments of charters not creating a new corporation.<sup>4</sup>

Reorganization.—The term "reorganization" has no very definite meaning in the law of corporations, but is applied indifferently to various proceedings and transactions by which succession of corporations is brought about, and also to proceedings by which existing corporations are continued under a different organization without the creation of a new corporation. Etymologically, the term signifies nothing more than "the act or process of organizing anew." The effect of the reorganization in any particular case must depend upon the intention of the parties, and the terms of the statute under which it is effected.

Generally, a reorganization is effected by the dissolution of an existing corporation, and the organization of an entirely new and distinct corporation to take its property and franchises, and continue its business.<sup>5</sup> This, however, is not necessarily the effect of a reorganization. The terms of the statute and the intention of the legislature and of the parties may be merely to continue the existing corporation, without any dissolution, under the same or a different name, and with the same or different powers, and under the same or a different management. In such a case there is a reorganization, but not, in the proper sense, a reincorporation. The identity of the corporation is not affected.<sup>6</sup>

Consolidation.—The consolidation of corporations is where two or more corporations are united into one. This may be effected by the dissolution of all the old corporations, and the creation of an entirely new and distinct corporation; or by the merg-

<sup>4</sup> See Miller v. English, 21 N. J. State v. Sherman, 22 Ohio St. 413; Law, 317. post, § 339.

<sup>&</sup>lt;sup>5</sup> Houston & Texas Central R. Co.
v. Shirley, 54 Tex. 125; Bruffett v.
<sup>6</sup> Miller v. English, 21 N. J. Law,
Great Western R. Co., 25 Ill. 353; 317; post, \$ 339.

ing of one or more corporations in another, the former only being dissolved. The consolidation of corporations will be separately considered at some length in a subsequent subdivision.

### § 336. Power of corporation to transfer property and franchises.

The power of a corporation to transfer its property and franchises, and its power to mortgage the same, have been considered at length in treating of the powers of corporations in a former chapter.

We have seen that a purely private corporation, as distinguished from a quasi public corporation owing special duties to the public, may transfer all its property to another corporation or person, and abandon its business, if the exigencies of its business make it advisable, distributing the proceeds of its property among its stockholders, after payment of its debts; but it cannot do so in fraud of its creditors. And if a corporation sells and transfers its property to another corporation, or to a natural person to be by him transferred to another corporation, organized or to be organized, it may, with the consent of all its stockholders, take in payment therefor shares of stock in the other corporation, if creditors are not prejudiced, and if the stock is taken for the purpose of distributing it among its stockholders, and not for the purpose of the corporation's holding it itself, and thus continuing its existence and business, through the instrumentality of the other corporation.8

We have also seen that a corporation cannot transfer its franchise to be a corporation without legislative authority; and that, according to the weight of authority, a railroad company or other quasi public corporation, owing special duties to the public in return for its franchises, cannot transfer its franchises other than its franchise to be a corporation, or its property necessary for the transaction of its business, and thereby render itself unable or less able to perform its duties to the

<sup>7</sup> Post, § 337 et seq. 8 Ante, §§ 160, 194(e).

public, unless such power has been conferred upon it by the legislature.9

In most jurisdictions, however, if not in all, express provision is made for the transfer of its property and franchises by a corporation, whether purely private or quasi public, under certain conditions, for a mortgage thereof, and for a sale thereof under an execution or on foreclosure of a mortgage. 10

#### § 337. Authority to reincorporate or reorganize.

The right of the members of a corporation to reincorporate. or of the members or members and creditors of a corporation to reorganize, like the right to incorporate in the first instance, 11 can only exist by virtue of authority from the legislature.12 In most states, if not in all, such authority has been granted by the legislature under certain conditions.\* And under some circumstances it exists under the general laws authorizing the formation of corporations.

When a corporation has been illegally or ineffectually organized, a new corporation may be formed, under a general law authorizing the formation of corporations for such purposes,

9 Ante, §§ 162, 163.

10 Ante, § 163(b).

11 Ante, § 37 et seg.

12 See State v. Steele, 37 Minn. 428; People v. De Grauw, 62 Hun (N. Y.) 224, 133 N. Y. 254; People v. James, 5 App. Div. (N. Y.) 412. Under the business corporations law of New York (Laws 1892, c. 691), providing (section 4) that any corporation may reincorporate on filing a certificate which shall contain the statement required by section 2, and that from the time of such filing "it shall have and exercise all such rights and franchises as it had and exercised under the laws pursuant to which it was originally incorporated," but making no provision for extending the

of incorporation shall state the object for which the corporation is formed, and the number of shares of capital stock, and that its duration shall not be more than 50 corporation years,-an existing cannot reincorporate for a period longer than that prescribed by its original charter, or make any change in its business. People v. James, 5 App. Div. 412.

\*An electric light, heat, and power company is a manufacturing corporation, within the Pennsylvania statute providing that, whenever the property and franchises of a manufacturing company shall be sold under process of court, the purchasers may reorganize the company. Com. v. Keystone Electric Light, Heat & Powterm of its corporate existence, or er Co., 193 Pa. St. 245. And see for changing its business; and pro- ante, § 36, as to the statutory viding (section 2) that a certificate classification of corporations.

to carry out the enterprise.13 The fact that some of the old corporators do not take stock in the new company is no ground for objection by the state.<sup>14</sup> A statute authorizing the reincorporation of "any existing corporation, association, or society incorporated" under the laws of the state, authorizes the incorporation of associations whose attempted incorporation under prior laws was unauthorized and ineffectual.<sup>15</sup>

Under a statute authorizing reincorporation of any corporation which has been dissolved by means of any nonuser or neglect to exercise any of the powers necessary for its preservation, a formal dissolution is not a condition precedent to the right to reincorporate. It is sufficient if the corporation has become practically dissolved by a failure to elect trustees.<sup>16</sup>

When the property and franchises of a corporation, as of a railroad company, turnpike company, etc., are sold under a mortgage thereon, or at any other judicial sale, or under execution, the purchasers are generally expressly authorized by statute to reorganize the corporation, but a statute expressly applicable to such cases is not necessary. In the absence of express restrictions, they may organize a corporation under the general laws authorizing the formation of corporations for such purposes. And the right to organize under a general law is not taken away by a special statute authorizing reorganization under such circumstances.17

The directors of a corporation cannot bind the members by proceedings to reincorporate or reorganize under a statute, unless authorized by them, or unless their proceedings have been ratified. But where the directors have performed the acts prescribed by the statute, for the purpose of effecting a reorganization or reincorporation, and the association has acted as a

<sup>13</sup> State v. St. Paul & Morris- Church v. Brownell, 5 Hun (N. Y.) town Turnpike Co., 92 Ind. 42.

<sup>14</sup> State v. St. Paul & Morristown Turnpike Co., 92 Ind. 42.

<sup>15</sup> State v. Steele, 37 Minn. 428.

<sup>16</sup> First Society of Irving M. E. And see post, § 345(h)(4).

<sup>17</sup> Moore v. State, 71 Ind. 478; State v. Hare, 121 Ind. 308. See, also, Vicksburg, Shreveport & Pac. R. Co. v. Elmore, 46 La. Ann. 1237.

corporation in pursuance thereof, it will be presumed that their action was authorized, until the contrary is made to appear.<sup>18</sup>

A statute authorizing persons who may purchase the property and franchises of railroad companies or other corporations at foreclosure sales, or other judicial sales, to organize a corporation to receive and hold the property and franchises purchased, does not, before it is acted upon, create any contract between the state and the holders of mortgage bonds of such corporations, or future purchasers at such sales, so as to prevent the legislature from repealing or changing the statute, or providing that a tax shall be paid on such a reorganization.<sup>19</sup>

#### § 338. Transfer as a dissolution.

A transfer of all its property and franchises by a corporation does not necessarily dissolve the corporation, for a corporation may exist without any assets at all. Nor is a corporation necessarily dissolved by a sale of its property and franchises under an execution, or on foreclosure of a mortgage. This has been shown at length in another chapter.<sup>20</sup>

As we have seen, however, a corporation may surrender its charter and dissolve with the consent of the state. And the terms of a statute authorizing a corporation to transfer its property and franchises, or authorizing their sale under execution or foreclosure, may be such that the transfer will operate as a dissolution. The question depends upon the intention.<sup>21</sup>

# § 339. Whether an old corporation is continued or a new corporation created.

(a) In general.—As we shall presently see at some length, if a statute and proceedings thereunder have the effect of merely continuing the existence of a corporation, although it may be with somewhat different powers, and under a different name,

 <sup>18</sup> State v Steele, 37 Minn. 428.
 20 Ante, § 310.
 19 People v. Cook, 148 U. S. 397.
 21 Ante, § 308.

and a different management, without destroying its identity as a corporate body, it is clear that rights and liabilities acquired or incurred by it before the change are not in any way affected.<sup>22</sup> But it is very different when an existing corporation is dissolved and ceases to exist, and an entirely new and distinct corporation is created.<sup>23</sup> It is often important, therefore, and sometimes as difficult as it is important, to determine whether there is a mere continuation of an existing corporation, without change of identity, or the creation of a new and different corporate body.

(b) Reorganization creating new corporation.—The term "reorganization" does not necessarily imply that a new corporation is created. Nor, on the other hand, does it necessarily imply that an old corporation is merely continued. Its effect in any particular case must depend upon the intention of the parties and the terms of the statute under which it takes place. Generally, no doubt, a reorganization is effected by the dissolution of an existing corporation, and the creation or formation of an entirely new and distinct corporation.<sup>24</sup>

If the property, or property and franchises, of a corporation are about to be sold at a sale under an execution against it, or at a sale under a power in a mortgage, or under a decree foreclosing a mortgage, or at any other judicial sale, the stock-

Law, 317; National Exchange Bank v. Gay, 57 Conn. 224; post, § 342(j).

<sup>23</sup> Bruffett v. Great Western R. Co., 25 Ill. 353; Bellows v. Hallowell & Augusta Bank, 2 Mason, 31, Fed. Cas. No. 1,279; post, § 342, and many cases there cited.

22 Miller v. English, 21 N. J. v. Weller, 93 Va. 605; Clough v. Rocky Mountain Oil Co., 25 Colo. 520; National Foundry & Pipe Works v. Oconto City Water Supply Co., 105 Wis. 48; post, § 342.

Where  $\mathbf{a}$ mining leased its property for five years, the lessee agreeing to organize a company and assign the lease to it, 24 See Houston & Texas Central the stock in the new company to be R. Co. v. Shirley, 54 Tex. 125; offered to the stockholders of the Bruffett v. Great Western R. Co., lessor, it was held that the new 25 Ill. 353; Morgan County v. company was not identical with Thomas, 76 Ill. 120; Atkinson v. Ma- the old, and that the statutory rietta & Cincinnati R. Co., 15 Ohio liens of persons furnishing supplies St. 21; State v. Sherman, 22 Ohio to it did not attach to the lessor's St. 411; Marshall v. Western North title. United Mines Co. v. Hatch-Carolina R. Co., 92 N. C. 322; Suer (C. C. A.) 79 Fed. 517, reversing preme Lodge, Knights of Pythias, 75 Fed. 368. holders or creditors, or any other persons, may organize a corporation under a general law for the purpose of purchasing at such sale, and continuing the business. When the scheme is carried out, and the transfer made, the purchasing corporation is clearly a new corporation, succeeding to the property and franchises purchased by it, and entirely distinct from the old The same is true, of course, where natural percorporation.25 sons purchase at such a sale, and afterwards form a corporation to take a transfer from them.26

Where an act of the legislature provided that, upon the happening of a certain contingency, the stockholders of a railroad company should "reorganize the said company as a new corporation," changed the amount of the capital stock, and provided for the stockholders of the existing corporation by reserving for them a certain amount of the stock of the new corporation, it was held that the reorganization created an entirely new and distinct corporation.27

Where an act of the legislature provided that the trustees in a deed of trust given by a railroad company upon its franchises, road, and property connected therewith, and the cestuis que trust and their associates, who should thereafter purchase at the sale under the deed of trust, should be incorporated by a name different from that of the old company, with power to purchase and own the franchises and property of the old company, and upon such purchase should be invested with all the corporate powers, privileges, etc., before given to the old company, but did not give the stockholders of the old company any rights in the new, or require the new company to pay the debts of the old, it was held that the effect of the legislation and reorganization thereunder was to create a new and distinct corporation, capable of purchasing, owning, and using

<sup>25</sup> People v. Cook, 110 N. Y. 443; Ferguson v. Ann Arbor R. Co., 17 App. Div. (N. Y.) 336; Gulf, Colorado & S. F. Ry. Co. v. Newell, 73 Tex. 334, 15 Am. St. Rep. 788; Midland Ry. Co. v. Fisher, 125 Ind. 19, 21 Am. St. Rep. 189; post, § 342(c). Carolina R. Co., 92 N. C. 322.

<sup>26</sup> Kittel v. Augusta, Tallahassee & G. R. Co., 78 Fed. 855; Lawrence v. Morgan's Louisiana & Texas R. & S. Co., 39 La. Ann. 427, 4 Am. St. Rep. 265.

<sup>27</sup> Marshall v. Western North

what was conveyed by the deed of trust, and not merely to continue the old corporation.28

(c) Reorganization merely continuing old corporation .- The terms of the statute under which a corporation is reorganized, and the intention of the parties, may be such as to merely continue the existing corporation without any change in the identity of the body, even though the powers of the corporation as reorganized may be different from the powers which it hadbefore the reorganization. Whether this is so depends upon the intention.29

Where an incorporated religious society elected new trustees and reorganized under a general law authorizing such societies to reincorporate, and conferring somewhat larger powers, and it appeared that their intention was not to create a new and distinct corporation, but merely to continue the old one, the intention was given effect, and it was held that the reincorporation did not create a new corporation.30

(d) Extension or revival of charters.—The extension and revival of charters has been somewhat considered in a former chapter.31 As was there stated, a mere extension of the charter of a corporation before its expiration, whether by a special act or under a general law, does not have the effect of creating a new and distinct corporation, unless such an intention appears, but merely continues the existence of the old corporation, without in any way affecting its identity or its existing rights and liabilities.32 This is true of an extension of the

<sup>&</sup>lt;sup>29</sup> Miller v. English, 21 N. J. Law, 317; First Society of Irving M. E. Church v. Brownell, 5 Hun (N. Y.) 464; Wilson v. Chesapeake & Ohio R. Co., 21 Grat. (Va.) 654.

<sup>30</sup> Miller v. English, 21 N. J. Law. 317.

<sup>31</sup> Ante, § 58.

<sup>32</sup> National Exchange Bank v. Gay. Minn. 372.

<sup>28</sup> Morgan County v. Thomas, 76 57 Conn. 224; St. Philip's Church v. Zion Presbyterian Church, 23 S. C. 297; People v. Marshall, 6 Ill. 672; Frostburg Mining Co. v. Cumberland & Pennsylvania R. Co., 81 Md. 28; Lincoln & Kennebec Bank v. Richardson, 1 Me. 79, 10 Am. Dec. 34; Town of Port Gibson v. Moore, 13 Smedes & M. (Miss.) 157. See, also, Cotton v. Mississippi & Rum River Boom Co., 22

period of existence of a national bank by or under an act of congress.33

A like construction has been placed by the courts upon statutes reviving the charter of a corporation after the period of its existence has expired.<sup>34</sup> It must be conceded, however, that it is not very clear how, when a charter has expired, and a corporation has thereby been dissolved and ceased to exist,<sup>35</sup> it can be said that a statute reviving the charter does not create,—recreate,—rather than continue, the corporation. If it creates instead of merely continuing a corporation for one purpose, it must do so for all purposes; and it has been held that such a statute is within a constitutional prohibition against the *creation* of corporations by special act.<sup>36</sup>

However this may be, the question is one of intention. A special act of the legislature, whether it is passed before or after the expiration of a charter, and whether it extends or revives the charter, or a general law providing for extension or revival, and proceedings thereunder, cannot be construed as merely continuing the old corporation, instead of creating a new one, if it affirmatively appears that the legislature and the corporators intended the creation of a new corporation.<sup>37</sup> "To ascertain," said Mr. Justice Story, "whether a charter created a new corporation, or merely continued the existence of an old one, we must look to its terms and give them a construction consistent with the legislative intent and the intent of the corporators."<sup>38</sup>

<sup>33</sup> National Exchange Bank v. Gay, 57 Conn. 224.

<sup>34</sup> St. Philip's Church v. Zion Presbyterian Church, 23 S. C. 297; People v. Marshall, 6 Ill. 672; Lea v. American A. & P. Canal Co., 3 Abb. Pr. (N. S.; N. Y.) 1; Phillips v. Town of Albany, 28 Wis, 340; Lincoln & Kennebec Bank v. Richardson, 1 Me. 79, 10 Am. Dec. 34; Town of Port Gibson v. Moore, 13 Smedes & M. (Miss.) 157; First Division of St. Paul & Pacific R. Co. v. Parcher, 14 Minn. 297.

<sup>36</sup> Ante, § 39(c)(4).

<sup>37</sup> Bellows v. Hallowell & Augusta Bank, 2 Mason, 31, Fed. Cas. No. 1,279; Young v. Rollins, 85 N. C. 485, 488; Marshall v. Western North Carolina R. Co., 92 N. C. 322, 330; Supreme Lodge, Knights of Pythias, v. Weller, 93 Va. 605; Huff v. Winona & St. Peter R. Co., 11 Minn. 180; Fitz v. Minnesota Central Ry. Co., 11 Minn. 414.

<sup>38</sup> Beliows v. Hallowell & Augusta Bank, 2 Mason, 31, 44, Fed. Cas. No. 1,279.

- (e) Amendment of charter.—As was pointed out in a former chapter, the mere amendment of the charter of a corporation, either by special act or under a general law, does not destroy the corporation and create a new one, but merely changes the constitution or powers of the old corporation; and therefore it does not in any way affect the existing contract or property rights of the corporation, or its existing obligations.<sup>39</sup>
- (f) Grant of special charter to an existing corporation.—We have also seen that, where a corporation which has been formed under a general law is afterwards granted a charter by a special act, and accepts the same, or a new charter is granted to a corporation existing under a special act, this does not necessarily constitute the creation of a new corporation, but may be, in effect, nothing more than an amendment of the original charter.40
- (g) Change or retention of name.—A mere change in the name of a corporation is a mere amendment, and does not in any way affect the identity of the corporation. This has repeatedly been held.41 On the other hand, where a corporation is reincorporated or reorganized, the fact that it retains the name of the old corporation does not make it the same. It is nevertheless an entirely new and distinct corporation, if such is the intention of the legislature and the corporators.42

## § 340. Whether purchasers become a corporation.

As was stated in a former chapter, the franchise to be a corporation is not transferable by a corporation without legis-

39 Trustees of University v. Moody. 62 Ala. 389; Dean v. La Motte Lead Co., 59 Mo. 523; Johnston v. Crawley, 25 Ga. 316, 71 Am. Dec. 173: Washington College v. Duke, 14 Iowa, 14. And see, infra, this section.

40 Johnston v. Crawley, 25 Ga. 59 Tex. 623; Dean v. La Motte 316, 71 Am. Dec. 173; Woodfork v. Lead Co., 59 Mo. 523; Higgins v. Union Bank of Tennessee, 3 Cold. California Petroleum & Asphalt (Tenn.) 488. Compare, however, Co., 122 Cal. 373; ante, § 55. Snook v. Georgia Improvement Co., 42 Marshall v. Western North 83 Ga. 61; Youngblood v. Georgia Carolina R. Co., 92 N. C. 322. And

Improvement Co., 83 Ga. 797; Carlisle v. Terre Haute & Richmond R. Co., 6 Ind. 316.

41 Trustees of University Moody, 62 Ala. 389; First Society of Irving M. E. Church v. Brownell, 5 Hun (N. Y.) 464; Acres v. Moyne,

lative authority. Although a corporation may be authorized to sell and convey to others its property and franchises, and may do so in pursuance of such authority, or although the property and franchises of a corporation may be sold, under legislative authority, by virtue of an execution against it, or under a decree foreclosing a mortgage, the purchasers do not become a corporation merely by virtue of the purchase and transfer, unless the legislature expressly so provides; but they can become so only by procuring a special act of incorporation, or by organizing under a general law, and then transferring the property and franchises to the corporation thus created.43

It is within the power of the legislature, however, subject to constitutional limitations, if any are applicable, to permit and provide for a transfer of the right to be a corporation. When a corporation, in pursuance of an act of the legislature, transfers its property and franchises, including the franchise to be a corporation, the transaction, in legal effect, is a surrender or abandonment of its charter by the corporation, with the consent of the legislature, and a grant by the legislature of a similar charter to the transferees, as of the time of the transfer 44

Where a statute authorized the sale of the state canals, and provided that the grantees should "hold and enjoy the same, together with all the rights, privileges, and franchises" of the grantors, who were a corporation, "and under such corporate name as said grantees" might adopt, it was held that an association of individuals purchasing the property became a corporation by virtue of the statute.45

The question as to what words are sufficient to show an in-

<sup>57, 7</sup> Am. Dec. 194; Bellows v. Hallowell & Augusta Bank, 2 Mason, 31, Fed. Cas. No. 1,279.

<sup>48</sup> Ante, § 37(f); Memphis & Little Rock R. Co. v. Railroad Com- v. Com., 50 Pa. St. 399.

see Memphis Water Co. v. Magens, missioners, 112 U.S. 609, 1 Keener's 15 Lea (Tenn.) 37; Wyman v. Hal- Cas. 112; Chaffe v. Ludeling, 27 lowell & Augusta Bank, 14 Mass. La. Ann. 607; State v. Morgan, 28 La. Ann. 482.

<sup>44</sup> State v. Sherman, 22 Ohio St. 411.

<sup>45</sup> Delaware Division Canal Co.

tention to create a corporation has been considered in a former chapter.46

- § 341. Property, rights, powers, franchises, and privileges of succeeding corporation.
- (a) Property and rights in general.—When one corporation sells and transfers its property to another, any question as to what property or rights pass depends, of course, upon the terms of the transfer, assuming that it is valid. And the terms of a mortgage by a corporation determine what property and rights pass to a purchaser at a foreclosure sale under the mortgage. If the transfer or mortgage covers all the assets of the corporation, the purchaser acquires all the assets that are transferable.\*

Where a railroad company mortgages its road and all its effects, under legislative authority, and the mortgage is foreclosed, the purchasers, afterwards incorporated under a new name, succeed to all the rights of the old company under a deed conveying a right of way for the construction of the road.47

-Property not covered by mortgage.-When the property of a corporation is sold under a mortgage, no property or rights can pass except such as are covered by the mortgage. a railroad company's road and all its rights, privileges, immunities, and franchises were sold under a decree foreclosing a mortgage, and the legislature afterwards incorporated the purchasers, and vested them with all the rights, title, interest, property, possession, claim, and demand at law or in equity, of, in, or to such road, with its appurtenances, and with all the rights, powers, immunities, privileges, and franchises of the former company, it was held that the new company ac-

<sup>46</sup> Ante, § 43. \* Pollard v. Maddox, 28 Ala. 321. v. Page, 35 Ark. 304.

Where a railroad company succeeds, by reorganization and purnew corporation to attack comprochase, to the property of another mise between old corporation and company, it cannot maintain an a subscriber for its stock, see action at law to recover property Whitaker v. Grummond, 68 Mich. of the old company which it had 249. conveyed to one of its directors.

Little Rock & Ft. Smith Ry. Co.

<sup>47</sup> Pollard v. Maddox, 28 Ala. 321,

quired no title to a judgment obtained by the old company, but which was not covered by the mortgage.<sup>48</sup>

—Property and rights which have vested in others on happening of contingency.—No property or right of a corporation can pass to another corporation succeeding to its property and rights, if, under a contract of the former corporation, the property or right has ceased to belong to it, and vested in another, by reason of its dissolution or the happening of other contingencies.

Where a telegraph company, incorporated for a certain number of years, contracted with a railroad company that so long as it should exist as a telegraph company it might erect and maintain a telegraph line within the limits of the railroad. and also that, in the event of the dissolution of the telegraph company or the suspension of operation, the railroad company might take charge of the telegraph line for its own purposes until the telegraph company should resume active operations, and that no interest of the telegraph company in the line should be assignable so as to affect or impair the rights of the railroad company under the agreement, and the telegraph company was reincorporated, just prior to the expiration of its term, under a new name, with new powers, and under different responsibilities, and under a charter which provided for the surrender of the old charter, it was held that its rights in and to the telegraph line were lost, and passed to the railroad company, though the new charter provided that all the property and assets of the former corporation, and all its debts, should devolve upon the new corporation, which for this purpose should be regarded as substituted by operation of law in place of the former corporation.49

—Continuing contracts—Termination of contract.—Whether a continuing contract terminates upon the reorganization of the corporation by which it is made depends, of course, upon the terms of the contract, and the nature and effect of the reorgan-

<sup>48</sup> Higgins v. Downward, 8 49 Latrobe v. Western Tel. Co. of Houst. (Del.) 227. Baltimore, 74 Md. 232.

ization. It seems perfectly clear that a contract conferring rights upon a corporation so long as it shall exist must terminate when the corporation is dissolved, and cannot pass to an entirely new corporation succeeding to the property and rights of the corporation by purchase, or on a reorganization, though it will not be terminated by a mere amendment of the charter of the corporation, or by a reorganization which does not create a new and distinct corporation.50

It has been held that the rights under a continuing contract will pass to a reorganized corporation, even when it is technically a new corporation, if it is in reality a mere continuance of the original corporation.<sup>51</sup> Thus, where a street railroad company entered into a contract with another street railroad company to pay the latter a certain sum for the use of its track, the agreement to last during the terms of their respective charters or any extension thereof, and the latter company was reorganized under a different name by its stockholders for the express purpose of the new company's taking all its property, assuming its obligations, and continuing its business, and the old company was then dissolved, it was held that the contract was not terminated by the reorganization, and that the right to use the tracks passed to the reorganized corporation.52

v. St. Charles Street R. Co., 44 La. Ann. 1069.

St. Charles Street R. Co., 44 La.

Ann. 1069.

Under a Michigan statute authorizing the reorganization of a national bank as a state bank, and providing that all assets of a dissolved national bank should, by act of law, vest in and become the property of such state bank, it was held that, where a national bank was reorganized as a state bank, and the latter took all its paper and assumed all its liabilities, and continued the same board of directors, the state bank was substantially the same as the na-

50 See Canal & Claiborne R. Co. tional bank, and could enforce a St. Charles Street R. Co., 44 La. written authority held by the national bank for the indorsement of 51 Canal & Claiborne R. Co. v. commercial paper. First Commercial Bank of Pontiac v. Talbert. 103 Mich. 625.

> Where a corporation made an assignment after a person had contracted with it to furnish a certain number of staves, and on the trustee's sale its assets were purchased by a new corporation, it was held that the benefit of the contract passed to the new corporation, and it could maintain an action for breach thereof as successor. White River Stave Co. v. Emmerson, 67 Ark. 617.

52 Canal & Claiborne R. Co. v. St.

—Subscriptions.—The right of a corporation to transfer subscriptions to its capital stock, and the right of a corporation with respect to subscriptions to the stock of a corporation to the property, rights, and franchises to which it has succeeded by purchase or otherwise, including the rights in such cases with respect to subscriptions by municipal corporations, are treated in a subsequent chapter.

(b) Powers, franchises, privileges, and immunities of succeeding corporation.—When a corporation is created or organized to succeed, by purchase or otherwise, to the property and franchises of another corporation, its powers, franchises, privileges, and immunities depend upon the statute by or under which it is created or formed, and its articles of association, in so far as they are authorized by the statute, just as in any It is often expressly provided by the statute that other case.53 the new corporation shall have the same rights, powers, franchises, privileges, and immunities as the old corporation, and these, of course, must be ascertained from the charter or articles of the old corporation,54 including amendments of the charter previously made and accepted by it.55

When one corporation becomes the successor of another by transfer of its charter under legislative authority, and there is no express provision as to its powers, it can exercise such powers, and such powers only, as were conferred, expressly or impliedly, upon the other corporation.<sup>56</sup> And generally, in the

53 City of Savannah v. Steamboat Co. of Georgia, R. M. Charlt. (Ga.)

54 Mulloy v. Nashville & Decatur R. Co., 8 Lea (Tenn.) 427, and other cases hereafter cited.

55 Where an act amending the charter of a corporation, and providing that it should go into effect if a majority of the stockholders, at their first majority meeting, should agree thereto, was duly accepted, and afterwards a new corporation was

Charles Street R. Co., 44 La. Ann. chartered with all the rights, powers, and privileges, and subject to all the liabilities and restrictions, conferred by the charter of the first corporation, and all the amend-ments thereto, it was held that the amendment to the charter of the first corporation became a part of the charter of the new corporation without the action of a majority of the latter's stockholders accepting it at its first regular meeting. Mulloy v. Nashville & Decatur R. Co., 8 Lea (Tenn.) 427. 56 State v. Newman, 51 La. Ann.

833, 72 Am. St. Rep. 476.

absence of any provision to the contrary, a purchaser of the property and franchises of a corporation under legislative authority, either directly from the corporation, or at an execution or foreclosure sale, acquires the same rights, franchises, and privileges as were possessed by the corporation, and is subject to the same burdens and restrictions.<sup>57</sup>

Where a railroad company's franchises, privileges, and property were mortgaged and sold under the power of sale in the mortgage, under legislative authority, and conveyed by the purchaser to a new corporation organized for the purpose of taking the property and franchises and continuing the operation of the road, it was held that the new company occupied the place of the old company so far as its franchises, privileges. and powers were concerned, and that liability for stock killed by reason of failure to fence its road was determined by a provision in regard thereto in the charter of the old company, and not by the general corporation law.58

(c) Franchises passing with property.—A sale, under legislative authority, of property of a corporation, the value of which depends upon special franchises which the corporation has, as in the case of a sale of the road and other property of a railroad company, the value of which depends upon the franchise to operate the railroad,—vests the purchaser with the fran-This is true, in the absence of provision to the chises also.59 contrary, although the purchaser is a natural person; and he may organize a corporation, and transfer the property and franchises to it.60

It follows that the purchaser of a railroad, whether a natural person or a corporation, acquires the right to appropriate, un-

Co., 43 Mich. 594; Mobile & Montgomery Ry. Co. v. Steiner, 61 Ala. 559; Mulloy v. Nashville & Decatur R. Co., 8 Lea (Tenn.) 427; Daniels 59 Morgan v. Louisiana, 93 U. S. v. St. Louis, Kansas City & N. R. 217; Lawrence v. Morgan's Louisi-Co., 62 Mo. 43; Pennsylvania R. Co. ana & Texas R. & S. Co., 39 La. v. Sly, 65 Pa. St. 209; Campbell v. Ann. 427, 4 Am. St. Rep. 265.

Marietta & Cincinnati R. Co., 23 60 Lawrence v. Morgan's Louisi-

<sup>57</sup> City of Detroit v. Mutual Gas Ohio St. 188; Montgomery & West Point R. Co. v. Boring, 51 Ga. 582. 58 Daniels v. St. Louis, Kansas City & N. R. Co., 62 Mo. 43.

der the power of eminent domain, strips of land necessary for the construction of depots, cattle pens, coal bins, sheds, and the like, without which the road could not be successfully operated. The term "franchises," it was said by the supreme court of the United States, "must always be considered in connection with the corporation or property to which it is alleged to appertain. The franchises of a railroad corporation are rights or privileges which are essential to the operations of the corporation, and without which its road and works would be of little value; such as the franchise to run cars, to take tolls, to appropriate earth and gravel for the bed of its road, or water for its engines, and the like. They are positive rights or privileges, without the possession of which the road of the company could not be successfully worked" 62

(d) Strict construction in favor of the public.—As was explained in a former chapter, when a corporation claims under its charter any exclusive right or privilege, or any right or privilege as against the state, or otherwise as against the general public, the charter is to be construed strictly against the corporation, and in favor of the public, and such a right or privilege will not be held to exist unless it has been granted by the legislature in clear and unmistakable terms.<sup>63</sup>

This principle applies with full force when a corporation which has succeeded to the rights, franchises, and privileges of another corporation claims such a right or privilege enjoyed by the old company, as the right of exemption from taxation, the right of exemption from legislative control in matters affecting the public, etc.<sup>64</sup> It has been held, in effect, that even when a statute confers upon a corporation in general terms "all the rights, powers, franchises, and privileges" of another corporation, it should not be construed as conferring rights and

63 Ante, § 127(b)(2).

ana & Texas R. & S. Co., 39 La. Ann. 427, 4 Am. St. Rep. 265.

<sup>61</sup> Lawrence v. Morgan's Louisiana & Texas R. & S. Co., 39 La. Ann. 427, 4 Am. St. Rep. 265.

<sup>62</sup> Morgan v. Louisiana, 93 U. S. 17.

<sup>&</sup>lt;sup>64</sup> Covington & Lexington Turnpike Road Co. v. Sandford, 164 U. S. 578. See, infra, this section.

privileges which are detrimental to the public, unless there is something else to show that the legislature so intended.65

(e) Rates chargeable by railroad companies, etc.—It has been held that a provision in the charter of a railroad company, giving it the right to fix the rate of fares on its road within certain limits, is a term of the contract between the state and the corporation, and a corporate franchise which passes upon a sale of its property and franchises to another corporation empowered by its charter to make the purchase, and that it is no more subject to impairment by the state after its transfer than before.66

But in an Ohio case, where a railroad company chartered by a special private act was authorized to charge a certain rate of toll, and its road was purchased, under legislative authority, and operated by another corporation, it was held that the special privilege or franchise as to the rate of tolls did not so inhere in the road as to pass to the purchasing corporation, so as to give it the right to charge higher tolls than was permitted under the general law applicable to railroads generally.67

Since a statute is to be strictly construed when it is claimed that it confers rights or privileges against the state, it has been held that a statute dividing a turnpike company into two distinct corporations, controlling different portions of the road, and providing that each shall retain "all the powers, rights, and capacities" granted by the charter of the original company, does not pass to the new companies a right of exemption from legislative control of tolls which was reserved to the original company by its charter.68

If the charter of a corporation, whose property is purchased under legislative authority by another corporation or by a natural person, and afterwards transferred by him to another corporation, contains restrictions as to the rates which it may

<sup>65</sup> Covington & Lexington Turnpike Road Co. v. Sandford, 164 U. Ry. Co. v. Moore, 33 Ohio St. 384. S. 578; Phoenix Fire & Marine Ins. Co. v. Tennessee, 161 U. S. 174.

<sup>66</sup> Ball v. Rutland R. Co., 93 Fed.

<sup>67</sup> Pittsburgh, Cincinnati & St. L.

<sup>68</sup> Covington & Lexington Turnpike Road Co. v. Sandford, 164 U. S. 578.

charge for transportation, the restrictions, in the absence of provision to the contrary, attach to the property in the hands of the purchasing corporation.<sup>69</sup>

- (f) Exemptions from taxation.—Whether or not an exemption from taxation enjoyed by a corporation passes to a corporation succeeding to its property, franchises, and privileges, depends upon the intention of the legislature. As we have seen in another chapter, such an exemption does not pass unless an intention that it shall do so affirmatively appears; and such an intention is not shown by the mere provision that the new corporation shall have all the "powers, privileges, franchises, and immunities" of the old corporation. There must be something else to show that these terms were intended to include the exemption from taxation.<sup>70</sup>
- (g) Effect of constitutional prohibitions.—After the adoption of a constitutional prohibition against the granting of a particular franchise, privilege, or immunity to corporations, the legislature has no power to provide for a transfer of such a franchise, privilege, or immunity from one corporation to another, or to provide for its transfer to a corporation purchasing the property of the corporation enjoying the franchise, privilege, or immunity at a sale on execution or foreclosure. This principle has been generally applied to exemptions from taxation, but it must apply with equal force to other privileges or immunities.<sup>71</sup>

### § 342. Liabilities of succeeding corporation.

(a) In general.—As a general rule, a separate and distinct corporation, which has succeeded, by a valid purchase and transfer, to the property and franchises of another corporation, is not liable, merely by reason of its succession, for the general debts or on the general contracts of the other corporation. It is not liable at all for such debts or on such contracts, in the

<sup>69</sup> Campbell v. Marietta & Cincinati R. Co., 23 Ohio St. 168. v. Palmes, 109 U. S. 244. See ante, 70 Ante, § 299(b)(8). § 299(b).

absence of a special agreement to pay or assume the same, nor is the property in its hands liable to be subjected to the same. in the absence of a valid lien thereon, unless it affirmatively appears that the transfer of the property and franchises of the other corporation constitutes, in fact or in law, a fraud upon its creditors, or the circumstances attending the creation of the new corporation, and its succession to the property and franchises of the old corporation, are such as to warrant a finding that it is in reality a mere continuation of the old corporation.72

(b) Purchase at execution sale.—This principle clearly applies when a corporation purchases the property and franchises of another corporation at a sheriff's or marshal's sale on an execution against the latter, and receives a conveyance in pursuance thereof. If the sale is authorized by law, the corporation takes the property free from any liability for existing debts of the other corporation, not secured by prior liens,

72 Austin v. Tecumseh Nat. Bank, 49 Neb. 412, 59 Am. St. Rep. 543; Bruffett v. Great West-ern R. Co., 25 Ill. 353; Morgan County v. Thomas, 76 Ill. 120; Memphis Water Co. v. Magens, 15 Lea (Tenn.) 37; Donnally v. Hearndon, 41 W. Va. 519; McLel-Ian v. Detroit File Works, 56 Mich. 579; Chesapeake, Ohio & S. W. v. Chesapeake & Ohio Canal Co., 14 Pet. (U. S.) 45; Houston & Texas Central R. Co. v. Shirley, 54 Tex. 125; Hopper v. Moore, 42 Tex. 125; Hopper v. Moore, 42 the property, rights, and interests Iowa, 563; Gulf, Colorado & S. F. of the corporation which issued Ry. Co. v. Newell, 73 Tex. 334, 15 the stock. Huggins v. Milwaukee Am. St. Rep. 788; Ewing v. Composite Brake Shoe Co., 169 Mass. 72; Warfield v. Marshall County sorbs all the assets of an old corporation, 263; Midland Ry. Co. v. poration, and continues to do business. Through y. Milwaukee Brewson contracted, as a principal is 189; Huggins v. Milwaukee Brewson contracted, as a principal is ing Co., 10 Wash. 579; Fitz v. liable for the acts of his agent. Minnesota Central Ry. Co., 11 Davis Provision Co. v. Fowler Minn. 414; Neff v. Wolf River Bros., 20 App. Div. 626, affirmed Boom Co., 50 Wis. 585; Chase v. 163 N. Y. 580.

Michigan Telephone Co., 121 Mich. 631; Pennison v. Chicago, Milwaukee & St. P. Ry. Co., 93 Wis. 344; National Foundry & Pipe Works v. Oconto City Water Supply Co., 105 Wis. 48; and other cases cited in the notes following.

An action for damages for the value of stock in a corporation, based upon a refusal to transfer R. Co. v. Griest, 85 Ky. 619; Smith the same on its books, cannot be maintained by a stockholder or his assignee against another corporation, which has succeeded to all the property, rights, and interests

and from all obligations of the other corporation of a strictly personal character.78

Where a person buys the property of a railroad company at a sale on execution against it, and conveys the same to a corporation, the latter is not liable to creditors of the old corporation for or on account of the price paid at the execution sale.74

(c) Purchase at foreclosure or other judicial sale.—It is equally clear that the rule applies when a corporation purchases the franchises and property of another corporation at a sale under a decree foreclosing a mortgage thereon, or other judicial sale, or where natural persons purchase at such sale, and afterwards transfer to a corporation.75

73 Gulf. Colorado & S. F. Ry. Co. v. Newell, 73 Tex. 334, 15 Am. St. Rep. 788.

74 Kittel v. Augusta, Tallahassee

& G. R. Co., 78 Fed. 855.

75 Midland Ry. Co. v. Fisher, 125 Ind. 19, 21 Am. St. Rep. 189; Moyer v. Fort Wayne, Cincinnati & L. R. Co., 132 Ind. 88; Lake Erie & Western Ry. Co. v. Griffin, 92 Ind. 487; Hoard v. Chesapeake & Ohio Ry. Co., 123 U. S. 222; Wiggins Ferry Co. v. Ohio & Mississippi Ry. Co., 142 U. S. 396; Sullivan v. Portland & Kennebec R. Co., 94 U. S. 806; Memphis Water Co. v. Magens, 15 Lea (Tenn.) 37; Pennsylvania Transportation Co.'s Appeal, 101 Pa. St. 576; Stewart's Appeal, 72 Pa. St. 291; Houston & Texas Central R. Co. v. Shirley, 54 Tex. 125; Morgan County v. Thomas, 76 Ill. 120; Hatcher v. Toledo, Wabash & W. R. Co., 62 Ill. 477; American Central Ry. Co. v. Miles, 52 Ill. 174; Vilas v. Milwaukee & Prairie du Chien Ry. Co., 17 Wis. 497; Smith v. Chicago & Northwestern Ry. Co., 18 Wis. 1; Gilman v. Sheboygan & Fond du Lac R. Co., 37 Wis. 317; City of Menasha v. Milwaukee & Northern R. Co., 52 Wis. 414; Neff v. Wolf River Boom Co., Royal & Augusta Ry. Co., 15 S. C. 10. 16 S. C. 567; Cook v. Detroit, of the sale, such a reorganized cor-

Grand Haven & M. R. Co., 43 Mich. 349; Ferguson v. Ann Arbor R. Co., 17 App. Div. (N. Y.) 336; National Foundry & Pipe Works v. Oconto City Water Supply Co., 105 Wis.

In an Indiana case, plaintiff, having agreed to erect a station for two railroad companies, each of which was to pay part of the cost, the balance to be paid by himself, built the station as agreed, but did not receive payment from one of the companies. Later this company's road was sold under a mortgage foreclosure, and bought in by the bondholders, who organized a new corporation to own and run it. The new corporation used the station, and the plaintiff sued it for the amount which the former owners of the road agreed to pay him. It was held that he could not re-Moyer v. Ft. Wayne, Cincover. cinnati & L. R. Co., 132 Ind. 88.

Under the Wisconsin statute providing that a person or association. becoming the owner or assignee of the rights, powers, privileges and franchises of a corporation under mortgage sale, may at any time within two years organize a new corporation, and have the same 50 Wis. 585; Hammond v. Port rights, privileges, and franchises as the old company had at the time

- (d) Sale under power in deed of trust.—The same rule applies to a sale under the power in a deed of trust given by a railroad company or other corporation, under legislative authority, to secure its bonds or other obligations. A corporation purchasing under such a sale takes the property and franchises conveyed by the deed of trust free from all debts of the other corporation not secured by a lien paramount to the deed of trust.76
- (e) Direct sale and transfer.—The general rule also applies, in the absence of fraud, actual or constructive, to a direct sale and transfer of its property and franchises by one corporation to another, authorized by its charter. If there is no fraud, and the purchasing corporation pays value, it is not liable for the general debts of the other corporation unless it assumes them. 77

the old corporation, but a new body, entitled to hold and enjoy the property formerly owned by the old corporation, free from the latter's liabilities, including liens against such property not prior to that through which the new corporation acquired title. National Foundry & Pipe Works v. Oconto City Water Supply Co., 105 Wis. 48.

A reorganized corporation, having the same officers and attorneys as the old, and succeeding to its property by purchase at a receiver's sale, is not a purchaser without notice of the rights in such property of parties to pending litigation between them and the old corporation involving the right to a lien on the property, and cannot relitigate in such suit questions which have been adjudicated as against the old corporation. Oregon Railroad & Navigation Co. v. Balfour (C. C. A.) 90 Fed. 295.

76 Morgan County v. Thomas, 76 111, 120,

poration is not a continuation of Iowa, 666, 2 Am. St. Rep. 263; Penthe old corporation, but a new body, nison v. Chicago, Milwaukee & St. P. Ry. Co., 93 Wis. 344; Chase v. Michigan Telephone Co., 121 Mich. 631; Goldmark v. Magnolia Metal Co., 44 App. Div. (N. Y.) 35. As to fraud, actual or construct-

ive, see infra, this section, (i).

Where a street railroad company issued to a person a pass for life, and afterwards sold its road to another company, it was held that the latter was not liable to an action for damages for refusal to recognize the pass, in the absence of an agreement to do so. Dallas Consolidated Traction Ry. Co. v. Maddox (Tex. Civ. App.) 31 S. W. 702; Eddy v. Hinnant, 82 Tex. 356.

In a late Michigan case it was said: "Even though the shareholders and officers of both corporations be the same, where no intention appears to transfer the old obligations to the new company, the new company is not liable, but creditors must look to the assets of the old company." And it was held 77 Chesapeake, Ohio & S. W. R. that proof that a corporation which Co. v. Griest, 85 Ky. 619; Wright had purchased all the property and v. Milwaukee & St. Paul Ry. Co., franchises of another corporation 25 Wis. 46; Tawas & Bay County owned nearly all the latter's stock R. Co. v. Iosco County Circuit at the time of the sale, that all the Judge, 44 Mich. 479; Warfield v. latter's employes continued in the Marshall County Canning Co., 72 former's employ after the sale, and

(f) Liability for torts.—Unless the case falls within one of the exceptions referred to in the paragraphs following, a corporation is not liable for the negligence or other torts of another corporation to whose property and franchises it has succeeded.<sup>78</sup> Thus, a corporation purchasing the property and franchises of a railroad company at a foreclosure or other judicial sale, or an execution sale, or from an individual who has purchased the same at such a sale, is not liable for damages to land adjoining the railroad, which accrued prior to the sale from improper drainage by reason of the old company's failure to properly construct its road.79

Where the property and franchises of a railroad company are purchased at a judicial sale, and the purchasers subsequently organize a corporation, the corporation is not liable for the operation of the road before it was organized and acquired possession and control.80

A corporation succeeding by purchase and transfer to the steamships of another corporation is not liable upon a judgment recovered against the other corporation for damages caused by a collision after the transfer.81

fore, did not show that the purchasing company assumed the selling company's liabilities. Chase v. Michigan Telephone Co., 121 Mich.

<sup>78</sup> Hammond v. Port Royal & Augusta Ry. Co., 15 S. C. 10, 16 S. C. 567; Neff v. Wolf River Boom Co., 50 Wis. 585; Pittsburgh, Cincinnati & St. L. Ry. Co. v. Fierst, 96 Pa. St. 144; Pennison v. Chicago, Milwaukee & St. P. Ry. Co., 93 Wis. 344; Chase v. Michigan Telephone Co., 121 Mich. 631.

79 Hammond v. Port Royal & Augusta Ry. Co., 15 S. C. 10, 16 S. C.

Where the property and fran-chises of a boom company were purchased at a bankruptcy sale, and the purchasers organized a boom company of the same name under Co., 115 U.S. 116.

that the business had been con- a statute which provided that the ducted in the same manner as be- purchaser at a bankrupt sale or other judicial sale of the property and franchises of a corporation created under the laws of the state might "reorganize under the charter, or act of incorporation, or law under which such company \* \* \* was created," and should have "the same rights, powers, privileges, and franchises that such company had at the time of the sale," it was held that the new company was not liable for injuries to a boat, caused by an obstruction which was placed in the river by the former company, but of the existence of which the new company had no notice. Neff v. Wolf River Boom Co., 50 Wis. 585.

80 Pittsburgh, Cincinnati & St. L. Ry. Co. v. Fierst, 96 Pa. St. 144.

81 Gray v. National Steamship

Of course, a corporation succeeding to the property of another corporation is liable for its own torts with respect to property received from the other corporation. Where a railroad company commits a trespass in taking and appropriating land, and constructing its road thereon, another corporation, which purchases its property and succeeds to its rights, and which takes possession of the land so taken, is equally a trespasser, and is liable to pay all damages occasioned by the trespass.82

(g) Special agreement to pay or assume debts or contracts.-The general rule that a corporation succeeding to the property and franchises of another corporation is not liable for the latter's general debts, or on its general contracts, does not apply where the succeeding corporation, by special agreement, assumes and promises to pay or perform such debts or contracts. In such a case it is liable by reason of its agreement or promise, for which its receipt of the property of the other corporation is a sufficient consideration. If the creditors of the old corporation assent to the change of liability, there is a clear novation, and they may in all jurisdictions maintain an action against the new corporation. Even in the absence of a novation, they may in most jurisdictions maintain an action on the promise of the new corporation, as being a promise made for their benefit.88 Of course, the agreement must be proved, and it must be shown that it was made by some person authorized to bind the corporation.84

& N. Ry. Co., 52 Iowa, 411.

88 Episcopal Charitable Society v. Episcopal Church in Dedham, 1 Pick. (Mass.) 372; Friedenwald v. And see Greene v. Middlesbor-Asheville Tobacco Works, 117 N. ough Town & Lands Co. (Ky.) 61 S. C. 544: Island City Savings Bank v. Sachtleben, 67 Tex. 420; Calu-

511; McKeefrey v. Connellsville Coke & Iron Co. (C. C. A.) 56 Fed. 212; First Nat. Bank of Chatta-nooga v. Radford Trust Co. (C. C. A.) 80 Fed. 569; Lake Erie & Western Ry. Co. v. Griffin, 92 Ind. 487.

W. 288.

84 Where the property and franmet Paper Co. v. Stotts Investment chises of a railroad corporation

- Debts or liabilities assumed. - If a corporation succeeds to the property and franchises of another corporation, and expressly agrees to assume all its debts or liabilities, it thereby assumes all its liabilities, of whatever nature. A railroad company which receives a transfer of the property and franchises of another company, under which it agrees to assume all the latter's liabilities, thereby assumes debts contracted by the latter for the construction of the lines of road transferred, and secured by a mortgage or deed of trust thereon.85

. The agreement, however, may specify the extent to which the succeeding corporation assumes the debts of the old corporation. And a general assumption of the debts of the old corporation may be restricted by an exception of particular debts. For example, where, upon the reorganization of a corporation, the new corporation took a bill of sale of the assets of the old corporation, in which it covenanted to pay all the debts and obligations of the old corporation "excepting" its mortgage bonds, it was held that it did not assume payment of the mortgage bonds.86

Where a continuing contract was made with a corporation by which the other party to the contract was to have control of the sales of its products, and a percentage thereof, and the corporation afterwards became incorporated under the laws of another state, retaining the same name, place of business, officers, and stockholders, and the new company purchased the property of the old company, and assumed its liabilities, it was held that the contract was a subsisting obligation which passed to the new company with other liabilities.87

have been sold and conveyed un- Paul & Pacific R. Co., 25 Minn. der a deed of trust, and the purchasers reorganize, there must be shown, in order to prove a new promise by the reorganized comcompany as originally organized, some action, on the part of former. Blake v. Domestic Mfg. the directors of the reorganized Co. (N. J. Eq.) 38 Atl. 241. company, from which the promise can be clearly inferred. American Central Ry. Co. v. Miles, 52 Ill. 174. 154 N. Y. 667.

85 Welsh v. First Division of St.

Where a corporation takes a transfer of all the assets of another corporation, and assumes all pany to pay a debt owing by the its debts, bondholders of the latter corporation become creditors of the

86 Fernschild v. Yuengling Brewing Co., 15 App. Div. (N. Y.) 29,

87 Reynolds v. Myers, 51 Vt. 444.

Of course, if a continuing contract with a corporation is such that by its terms it is terminated by a sale and transfer of the business and property of the corporation, the purchasing corporation does not assume any liability thereunder for any period after the sale and transfer. Where the by-laws of a corporation provided that the secretary should be elected for a year, subject to removal by the directors, and that his duties should be to keep the accounts of the corporation, and transact all its business, it was held that the term of office of the secretary terminated on a sale of its business by the corporation, and that the vendee, therefore, although it agreed to fulfill all the contracts of the corporation, was not liable to the secretary for his salary for the unexpired portion of the year for which he was elected.\*

Judgment in pending action.—When a corporation purchases the property and franchises of another corporation, and agrees to pay all its predecessor's "debts," it may be sued upon a judgment recovered against the old company in an action pending at the time of the transfer. It is not necessary that the suit against it be brought upon the original cause of action.<sup>88</sup>

—Statute of frauds.—Where a corporation transfers all its property to another corporation, and the latter, in consideration thereof, assumes all its debts, the agreement is an original one, and is not within the clause of the statute of frauds requiring a promise to answer for the debt of another to be in writing.<sup>89</sup>

Defenses of new corporation.—When a corporation which has succeeded to the property of another corporation, and assumed its liabilities, is sued upon a contract of the old company, it is in no better position as to the defenses which it may make than the old company would be. For example, though a lease made to a corporation may have been voidable

<sup>\*</sup>Union Compress Co.v. Douglass, 59 Calumet Paper Co. v. Stotts Investment Co., 96 Iowa, 147.
88 Noll v. Chattanooga Co. (Tenn. Ch. App.) 38 S. W. 287.

on the ground of fraud, yet, where it has ratified the same by acting under it and receiving the benefit of it, a corporation succeeding to its rights under the lease, under an agreement by which it assumes all its liabilities, cannot set up the fraud as a defense in an action to recover rents due under the lease.90

(h) Implied assumption of debts or other liabilities.—Ordinarily a promise on the part of a corporation to pay or assume the debts or other liabilities of another corporation cannot be implied from the fact that it has received the assets of the latter; 91 but there may be special circumstances which will give rise to an implied promise. If a corporation purchases the property and franchises of another corporation, whether directly from the latter, or at a mortgage foreclosure sale, and takes possession of all the property, including property for which the other corporation was under obligation to pay, and to which it could acquire no right without payment, the purchasing corporation impliedly assumes the obligation. ample, if a railroad company appropriates or condemns land for the purpose of its road, and a judgment is rendered against it for the value of the land, and a new corporation purchases, at a foreclosure sale or otherwise, and enters upon and occupies the land, including the right of way, it may be held liable to pay the judgment, on the ground that it has adopted and ratified the original appropriation.92

In order that a promise may be implied, on the part of a corporation, to pay the debts of another corporation, to the property and franchises of which it has succeeded by a valid purchase, the conduct relied upon must show such an intention. The mere fact that the new corporation has voluntarily paid some of the debts of the old corporation is no ground for inferring that it assumed the latter's debts.93

 <sup>80</sup> Barr v. New York, Lake Erie 18 Wis. 155, 86 Am. Dec. 751. And & W. R. Co., 125 N. Y. 263.
 18 Wis. 155, 86 Am. Dec. 751. And see supra (f), note 82.

<sup>91</sup> See the cases heretofore cited under this section, (a)-(f).

<sup>92</sup> Lake Erie & Western Ry. Co. v. Griffin, 92 Ind. 487; Pfeifer v.

see supra (f), note 82.

93 The fact that a new fair association, a corporation, bought an old fair association's grounds, and voluntarily paid premiums offered Sheboygan & Fond du Lac R. Co., by, and advertising claims against,

The fact that a new bank receives some of the notes or bills of an old bank of the same name, and reissues them, does not impose upon it liability to pay all the notes or bills of the old bank.<sup>94</sup>

(i) Transfers fraudulent as to creditors.—The rule that a corporation taking a transfer of the property and franchises of another corporation takes the same free from any liability for the general debts of the latter does not apply where the transfer constitutes, either in fact or as a matter of law, a fraud upon the creditors of the other corporation. In such a case, the creditors defrauded by the transfer may, in equity, follow the property into the hands of the new corporation, and subject it to the satisfaction of their claims, or hold the corporation liable to the extent of its value.<sup>95</sup> "Corporations cannot,

the latter, does not charge it with the latter's debts. Texas State Fair & Dallas Exposition Ass'n v. Caruthers, 8 Tex. Civ. App. 474.

94 Bellows v. Hallowell & Augusta Bank, 2 Mason, 31, Fed. Cas. No. 1,279; Wyman v. Hallowell & Augusta Bank, 14 Mass. 57, 7 Am. Dec. 194.

95 Hibernia Ins. Co. v. St. Louis & New Orleans Transp. Co., 13 Fed. 516, 4 McCrary, 432; Blair v. St. Louis, Hannibal & K. R. Co., 22 Fed. 36; Brum v. Merchants' Mutual Ins. Co., 16 Fed. 140; Chicago, Milwaukee & St. P. Rv. Co. v. Third Nat. Bank of Chicago, 134 U. S. 276; Fort Payne Bank v. Alabama Sanitarium, 103 Ala. 358; McVicker v. American Opera Co., 40 Fed. 861; Austin v. Tecumseh Nat. Bank, 49 Neb. 412, 59 Am. St. Rep. 543; Grenell v. Detroit Gas Co., 112 Mich. 70; National Bank of Jefferson v. Texas Investment Co., 74 Tex. 421; Couse v. Columbia Powder Mfg. Co. (N. J. Eq.) 33 Atl. 297; Booth v. Bunce, 33 N. Y. 139, 88 Am. Dec. 372; Cole v. Millerton Iron Co., 133 N. Y. 164; Hancock v. Holbrook, 40 La. Ann. 53; Montgomery & West Point R. Co. v. Branch, 59 Ala. 139; Blanc v. Paymaster Mining Co., 95 Cal. 524, 532, 29 Am. St. Rep. 149; Vance v. McNabb Coal & Coke Co., 92 Tenn. 47; First Nat. Bank of Chattanooga v. Chattanooga Pulley Co., 97 Tenn. 308; Barksdale v. Finney, 14 Grat. (Va.) 338.

See, also, Higgins v. California Petroleum & Asphalt Co., 122 Cal. 373; Smith v. Smith, Sturgeon & Co. (Mich.) 84 N. W. 144.

Where a new corporation took the assets of an old corporation. which was insolvent, and promised, in consideration thereof, to pay certain of its debts, and settled certain debts at a reduction by compromise, and suit was afterwards brought against it by a creditor of the old company to charge the assets in its hands with payment of the old company's debts, it was held that the fact that some of the debts had been compromised and settled for less than their face value would not be taken into consideration, and that the assets of the old company in the hands of the new would be treated as a fund for the payment of all the debts of the old company pro rata. First Nat. Bank of Chattanooga v. Chattanooga Pulley Co., 97 Tenn. 308.

Where a plan of reorganization

any more than individuals, relieve their property from the payment of debts, except by a sale or transfer in good faith and for a full consideration."96

If the stockholders of a corporation organize another corporation, and transfer all the assets of the former to the latter, without paying the debts of the former, the transfer, irrespective of the actual intent of the parties, constitutes a fraud upon the creditors of the old corporation, and the new corporation is liable in equity for the debts of the old to the extent of the assets received by it, or the assets themselves may be followed by the creditors of the old corporation, so long as they have not passed into the hands of bona fide purchasers for value.97 This applies with peculiar force where the members of the old corporation and the new are the same persons, or mostly so.98

If a corporation, being indebted, conveys all its property, upon a nominal or grossly inadequate consideration, and without making provision for its creditors, to a new corporation brought into existence through the agency of the officers of the old company, and for the sole purpose of the transfer, the transfer is fraudulent, as a matter of law, and without regard

is entered into and carried out by the stockholders and secured creditors of an insolvent corporation. pursuant to which all the property of the corporation is sold by foreclosure and otherwise, and transferred to the new corporation, the stockholders of the old corporation retaining their interest and rights. and by virtue thereof being either fraud is thereby perpetrated upon the unsecured creditors of the old corporation, so that they may hold the new corporation liable for their claims. Central of Georgia Ry. Co. v. Paul (C. C. A.) 93 Fed. 878.

96 Rorke v. Thomas, 56 N. Y. 563; Wabash, St. Louis & Pac. Ry. Co. v. Ham, 114 U. S. 594; Vance v. McNabb Coal & Coke Co., 92 Tenn. 47, 59.

97 Hibernia Ins. Co. v. St. Louis & New Orleans Transp. Co., 13 Fed. 516, 4 McCrary, 432; Harrison v. Arkansas Valley Ry. Co., 13 Fed. 522, 4 McCrary, 264; Montgomery Web Co. v. Dienelt, 133 Pa. St. 585, 19 Am. St. Rep. 663; Metcalf v. Arnold, 110 Ala. 180, 55 Am. St. Rep. 24; Slattery v. St. Louis & New Orleans Transp. Co., 91 Mo. stockholders in the new corpora- 217, 60 Am. Rep. 245; Booth v. tion, or otherwise provided for, a Bunce, 33 N. Y. 139, 88 Am. Dec. 372; Cole v. Millerton Iron Co., 133 N. Y. 164; Vance v. McNabb Coal & Coke Co., 92 Tenn. 47; Hancock v. Holbrook, 40 La. Ann. 53; Couse v. Columbia Powder Mfg. Co. (N. J. Eq.) 33 Atl. 297.

98 Montgomery Web Co. v. Dienelt, 133 Pa. St. 585, 19 Am. St. Rep. 663; Metcalf v. Arnold, 110 Ala. 180, 55 Am. St. Rep. 24; and other cases in the note preceding. to the actual intent of the parties; and the creditors of the old company may follow the assets into the hands of the new, if rights of innocent purchasers have not intervened.<sup>99</sup>

A corporation which acquires the entire property of another corporation under an arrangement which has the effect of distributing the assets of the latter among its stockholders in fraud of its creditors takes the property subject to the payment of all the debts of the vendor, including a judgment subsequently recovered against the latter in an action for negligence pending at the time of the transfer.<sup>100</sup>

Foreclosure sale.—Ordinarily, as we have seen, a sale under a decree foreclosing a mortgage on the property of a corporation, or under a power of sale therein, cuts off all rights of general creditors to follow the property. But this is not so where the foreclosure sale is fraudulent. Where the assets of a corporation are allowed by its directors to be sold under mortgages in order that they may be transferred by the nominal purchaser to a new corporation organized by the same directors, for the purpose of saving the assets from liability for other debts, the value of the assets being largely in excess of the mortgages, a court of equity will follow the excess, and compel its application to the debts of the old corporation. 102

Transfers not fraudulent.—When a corporation receives a transfer of all the property and franchises of another corporation in good faith, and pays a full consideration therefor, the transfer is not fraudulent as against the unsecured creditors of the old corporation, and they cannot follow and subject the property in the hands of the new corporation, or sue to set aside the transfer. It was so held, for example, where a corporation purchased all the assets of another corporation, and paid full value therefor by assuming and paying a debt secured by a mortgage thereon. 103

<sup>99</sup> Vance v. McNabb Coal & Coke Co., 92 Tenn. 47.

<sup>100</sup> Grenell v. Detroit Gas Co., 112 Mich. 70.

<sup>101</sup> See supra, this section, (c).

<sup>102</sup> Goddard v. Fishel-Schlichten Importing Co., 9 Colo. App. 306.

<sup>103</sup> Warfield v. Marshall County Canning Co., 72 Iowa, 666, 2 Am. St. Rep. 263.

A corporation purchasing the property of another corporation at a foreclosure sale or otherwise does not become liable for the debts of the latter merely because the stockholders of the old company become stockholders of the new without the payment of any money, where they do so by virtue of an arrangement subsequent to the purchase.<sup>104</sup>

Remedies of creditors.—The remedies of creditors of a corporation, the assets of which have been fraudulently transferred to another corporation, are not the same in all jurisdictions. For a full treatment of the subject, the reader must consult works dealing generally with fraudulent conveyances.

Generally the transfer in such cases, although fraudulent as against creditors, operates to transfer the title to the new corporation, and the remedy of the creditors of the old corporation is in equity, to set the transfer aside and subject the property to the payment of their claims, or to hold the new corporation liable to the extent of the property received by it. 105 An action at law cannot be maintained against the new corporation on a debt of the old, unless it has expressly assumed the same. 106

In some jurisdictions, however, the creditors of the old corporation may treat the transfer to the new corporation as an absolute nullity, and, if they have recovered judgment against the old corporation, they may levy an execution on the property, just as if there had been no transfer.<sup>107</sup>

Some of the courts have held that a creditor of the old corporation must obtain a judgment against it before he can come into a court of equity and attack the transfer to the new corporation as fraudulent.<sup>108</sup> But this is not true in all juris-

<sup>104</sup> Stewart's Appeal, 72 Pa. St. 291.

<sup>105</sup> Hibernia Ins. Co. v. St. Louis & New Orleans Transp. Co., 13 Fed. 516, 4 McCrary, 432; Ewing v. Composite Brake Shoe Co., 169 Mass. 72; Metcalf v. Arnold, 110 Ala. 180, 55 Am. St. Rep. 24; Citizens' Bank of Kingman v. McClelland, 53 Kan. 699; and other cases cited in the notes preceding.

<sup>106</sup> Ewing v. Composite Brake Shoe Co., 169 Mass. 72.

 <sup>107</sup> Montgomery Web Co. v. Dienelt, 133 Pa. St. 585, 19 Am. St.
 Rep. 663; Booth v. Bunce, 33 N. Y.
 139, 88 Am. Dec. 372.

But see Citizens' Bank of Kingman v. McClelland, 53 Kan. 699.

<sup>108</sup> Tawas & Bay County R. Co.

dictions. In a leading case in a federal court, where the stockholders of a corporation had organized another corporation and transferred all the assets of the former to the latter without consideration, it was held that a creditor of the former could maintain a suit in equity against the latter to recover a money judgment to the extent of the property received by it, without having first obtained a judgment at law against the former.<sup>109</sup>

In admiralty.—It has also been held that, where the members of a partnership or corporation form a corporation, and transfer to it, without any consideration, all the assets of the former partnership or corporation, without providing for payment of its debts, a creditor of the former partnership or corporation may, in a proper case,—as in the case of a claim for salvage services,—maintain a libel in admiralty against the new corporation to enforce his claim to the extent of the assets received by it.<sup>110</sup>

Bona fide purchasers.—When a corporation thus transfers its property in fraud of its creditors, their right to follow the same in equity, or in some states at law, 111 is superior to the rights of all persons who are not in the position of bona fide purchasers for value. 112 Their right is superior to any right of mortgagees of the new corporation with notice. 113 And it is superior to the rights of stockholders of the new corporation who have received their stock solely in consideration of their claims as creditors of the old corporation, for they are not in the position of bona fide purchasers. 114

v. Iosco County Circuit Judge, 44 Mich. 479.

When all the assets and franchises of a corporation are fraudulently transferred to another corporation, a liability of the old company founded on tort must be established against it by judgment before it can be enforced against the new company. Chase v. Michigan Telephone Co., 121 Mich. 631.

109 Hibernia Ins. Co. v. St. Louis & New Orleans Transp. Co., 10 Fed. 596, 3 McCrary, 368, 13 Fed.

516, 4 McCrary, 432. See, also, Blanc v. Paymaster Mining Co., 95 Cal. 524, 29 Am. St. Rep. 149.

110 Brum v. Merchants' Mutual Ins. Co., 16 Fed. 140.

111 See supra, this section.

112 Montgomery & West Point R. Co. v. Branch, 59 Ala. 139.

113 Montgomery & West Point R. Co. v. Branch, 59 Ala. 139; Blair v. St. Louis, Hannibal & K. R. Co., 24 Fed. 148; Cole v. Millerton Iron Co., 133 N. Y. 164.

114 Montgomery Web Co. v. Die-

A corporation which purchases the entire property of another corporation, and issues therefor its own stock to the stockholders of the other corporation, is not a bona fide purchaser as against creditors of the other corporation defrauded by the transfer. The fact that the new corporation assumes the debts of the old corporation does not make it a bona fide purchaser, so as to prevent a creditor of the old corporation from attacking the transfer as fraudulent, for creditors cannot be compelled to accept a change of debtors. 116

A corporation acquiring the entire property of another corporation under an arrangement which has the effect of distributing the latter's assets among its stockholders in fraud of its creditors is chargeable with knowledge of the arrangement and its purpose possessed by all its promoters and stockholders.<sup>117</sup>

A corporation which purchases all the property of another corporation, knowing that the other corporation is insolvent, under an arrangement by which the purchase price will be placed beyond the reach of creditors, if there are any, is under a duty to inquire as to the existence of unsecured creditors, and is chargeable with all knowledge which such an inquiry would disclose.<sup>118</sup>

(j) Mere continuation of corporation.—The rule that a corporation is not liable for the debts of another corporation, to whose property and franchises it has succeeded, clearly does not apply where the corporations are, in law, the same body. Where the charter of a corporation is merely amended, either by a special act or under a general law, there is no change in the identity of the corporate body,—no dissolution of one corporation and creation of another,—and the corporation, under the amended charter, is liable for all debts contracted by

nelt, 133 Pa. St. 585, 19 Am. St. 117 Grenell v. Detroit Gas Co., Rep. 663. 112 Mich. 70.

<sup>115</sup> Grenell v. Detroit Gas Co., 118 Chattanooga, Rome & C. R. Co. v. Evans (C. C. A.) 66 Fed. 116 Cole v. Millerton Iron Co., 809.

<sup>116</sup> Cole v. Millerton Iron Co., 809. 133 N. Y. 164.

it before the amendment. 119 The same is true where the charter of a corporation is merely extended or revived, or the corporation reorganized, without creating a new corporation, as was explained in a former section. 120

It seems to have been held that the general rule does not apply where the circumstances attending the creation of a new corporation, and its succession to the property, franchises, and business of another corporation, are such as to show that the new corporation is in reality, however it may be in law, a mere continuation of the old corporation; or, in other words, that, although technically, as a matter of law, a new corporation may be created, yet, if the old corporation ceases to exist, and all its assets and franchises are acquired by the new, which is in reality a mere continuation of the old, the new corporation is to be held to have impliedly assumed, and is liable upon, all the obligations of the old. 121 The true ground of liability, however, where, as a matter of law, the corporations are not the same, is fraud, either in fact or in law, as explained in a former section. 122

Moody, 62 Ala. 389; Johnston v. Crawley, 25 Ga. 316, 71 Am. Dec. 173; Dean v. La Motte Lead Co., 59 Mo. 523; Washington College v. Duke, 14 Iowa, 14. See ante, §

339(d), (e).
120 St. Philip's Church v. Zion Presbyterian Church, 23 S. C. 297; Lea v. American A. & P. Canal Co., 3 Abb. Pr. (N. S.; N. Y.) 1; Miller v. English, 21 N. J. Law, 317; Wil-son v. Chesapeake & Ohio R. Co., son v. Chesapeake & Ohio R. Co., Higgins v. California Petroleum & 21 Grat. (Va.) 654; Barksdale v. Asphalt Co., 122 Cal. 373. But see Finney, 14 Grat. (Va.) 338; National Exchange Bank v. Gay, 57 Conn. 224; People v. Marshall, 6 Ill. 672; Frostburg Mining Co. v. Iquidation as allowed by the na-Cumberland & Pennsylvania R. tional bank act, and was reorgan-Co., 81 Md. 28. And see ante, \$ ized as a state bank, taking all 339.

A corporation improperly organized which dissolves, and is legally Eans' Adm'r v. Exchange Bank of incorporated under a different name, cannot repudiate its paper issued before the dissolution. Em- Louis & New Orleans Transp. Co.,

119 Trustees of University v. pire Mfg. Co. v. Stuart, 46 Mich.

121 Reed v. First Nat. Bank of Weeping Water, 46 Neb. 168; Austin v. Tecumseh Nat. Bank, 49 Neb. 412, 59 Am. St. Rep. 543; Berry v. Kansas City, Ft. Scott & M. R. Co., 52 Kan. 774, 39 Am. St. Rep. 381; Thompson v. Abbott, 61 Mo. 176; Barksdale v. Finney, 14 Cret. (Vo.) 238; McVicker v. Grat. (Va.) 338; McVicker v. American Opera Co., 40 Fed. 861; Higgins v. California Petroleum &

the assets of the old corporation, it was held liable for its deposits.

As was shown in another section, a corporation is not the same as another corporation, to whose property and franchises it has succeeded, merely because it has the same name. 123 The fact that a corporation formed to purchase the franchises and property of another corporation at a mortgage foreclosure sale has the same name as the other corporation does not make it a mere continuation of the latter, so as to render it liable for its debts. 124 And the fact that a banking company is organized under the same name as that of a former company, that it appoints the same persons as officers, and that it receives and issues the notes of the former, does not make it a mere continuation of the former, so as to render it liable on its notes. 125

On the other hand, as we have seen, the fact that the name of a corporation is changed does not necessarily show that it is a different corporation after the change. A mere change in the name of a corporation does not affect its identity, and it is liable under the new name for debts contracted under the old. 126

(k) Liability imposed by statute.—Frequently a statute or charter authorizing a corporation to acquire the property and franchises of another corporation expressly provides that it shall be liable for the debts of the other corporation. corporation acts upon and accepts the benefit of the statute, it thereby agrees to its terms and conditions, and cannot escape the liability imposed. 127

13 Fed. 516, 4 McCrary, 432; Blanc v. Paymaster Mining Co., 95 Cal. 533, 724, 29 Am. St. Rep. 149; Chase v. Michigan Telephone Co., 121 Mich. 631.

And see supra, this section, (i). 123 Ante, § 339(g).

124 Memphis Water Co. v. Magens, 15 Lea (Tenn.) 37.

125 Wyman v. Hallowell & Augusta Bank, 14 Mass. 57, 7 Am. Dec. 194; Bellows v. Hallowell & Augusta Bank, 2 Mason, 31, Fed. Cas. No. 1,279.

126 Ante, § 339(g); Dean v. La Motte Lead Co., 59 Mo. 523;

62 Ala. 389; First Society of Irving M. E. Church v. Brownell, 5 Hun (N. Y.) 464; Acres v. Moyne, 59 Tex. 623.

127 New Bedford R. Co. v. Old Colony R. Co., 120 Mass. 397; Welsh v. First Division of St. Paul & Pac. R. Co., 25 Minn. 314; St. Louis, Alton & T. H. R. Co. v. Miller, 43 Ill. 199.

Of course, to render the corporation liable, the purchase must be made. In a suit against a railroad company on promissory made by another company, the Trustees of University v. Moody, fact that the defendant was au-

A corporation purchasing the property and franchises of another corporation at a foreclosure sale is not rendered liable for the debts of the latter by a provision in its charter that it shall be vested with all the latter's powers and privileges, and be subject to all its duties and liabilities. Such a provision merely imposes upon the new corporation the burdens and obligations imposed upon the old corporation by its charter. 128

It is not necessary that the statute shall provide any specific remedy in favor of creditors of the old corporation for enforcing their rights against the new. If no specific remedy is prescribed, the common-law remedies may be resorted to. For example, if a statute incorporating the purchasers of the franchises and property of a railroad company provides that the new company shall pay all unsatisfied judgments recovered against the old company, a judgment creditor of the latter, if his judgment is not paid, may maintain an action of debt thereon against the new company, for "where a statute imposes a duty or liability, the common law affords the remedy by the ordinary action of debt, when the demand is for a sum certain, or assumpsit, as the case may be." 129

If a statute imposes such liability for all claims or demands, or in other general terms, it is answerable, not only for liabilities arising out of contract, but also for liabilities arising out of tort, as for the conversion of property, fraud, or negligence. In a Minnesota case, under a statute providing that a railroad company succeeding by purchase and transfer to the franchises and property of another company should assume all claims and demands of the latter, it was held that the new company was liable in an action to recover damages for the illegal procurement and negotiation of certain bonds by the old company. 130

notes, on condition that it should pay the debts of the latter, will not gens, 15 Lea (Tenn.) 37. be sufficient to make the defend
129 St. Louis, Alton & T. H. R. be sufficient to make the defendant liable. It must further be Co. v. Miller, 43 Ill. 199. shown that the defendant purchased the road of the other com- & St. Peter R. Co., 36 Minn. 505.

thorized by law to purchase the pany. Desmond v. St. Louis, Alroad of the company making the ton & T. H. R. Co., 77 Ill. 631. notes, on condition that it should 128 Memphis Water Co. v. Ma-

130 Town of Plainview v. Winona

Where a statute authorized a railroad company to purchase the rights, franchises, and property of another railroad company, and authorized the latter to sell and convey to the former its franchises and property, rights, easements, privileges, and powers, and declared that thereupon the former should "be subject to all the duties, liabilities, obligations and restrictions to which" the latter might be subject, and the purchase and transfer were made, it was held that the purchasing corporation became directly liable in an action of tort for damage occasioned by the prior neglect of the selling corporation. "The privity necessary to support the action," said the court, "is created by the statute and the purchase and conveyance under it." 131

(1) Obligations and covenants running with the property acquired.—The general rule that a corporation succeeding to the property and franchises of another corporation is not liable for the debts or contracts of the latter, unless it expressly agrees to assume the same, 132 does not apply to obligations and covenants of the other corporation which adhere to and run with the property acquired. These are binding upon the purchasing corporation, whether it expressly assumes them or not, if it takes possession of and uses the property.

In a late Indiana case, where a railroad company had, in a deed conveying to it a right of way, agreed to build a fence along the same, and the right of way, together with its other property and franchises, was purchased by another company at a sale under a decree foreclosing a mortgage thereon, it was held that the right of the original grantor to have the fence built was not a mere general right against the grantee corporation, not enforceable against the corporation purchasing at the foreclosure sale, but was a right blended with the right to use and occupy the land, that the grantee's covenant to construct the fence was a covenant running with the land, and that the

 $<sup>^{131}\,\</sup>mathrm{New}\,$  Bedford R. Co. v. Old  $^{132}\,\mathrm{Supra},$  this section, (a)-(f). Colony R. Co., 120 Mass. 397.

purchasing corporation, in taking and occupying the land, became bound to perform the same.

The court said in this case: "We regard the performance of the agreement to build a fence as a condition of the right to enjoy the easement granted by the owners of the land. right which the appellee seeks to enforce is more than a general claim for money, for it is a right blended with that of the appellant to use and occupy the land with its track. The appellant's liability does not rest upon the claim against the old company, but upon the duty which arises out of the occupancy of the land. It cannot, in equity, be permitted to enjoy the easement, and yet refuse to perform the agreement which created and conferred the easement. \* \* The appellant is in the possession of the right of way as the grantee of the original contractor, and it must take the benefit it enjoys subiect to the burden annexed to it by the contract which gave existence to that benefit. It cannot enjoy the benefit and escape the burden, for the burden and the benefit are so interlaced as to be inseparable. One who takes a privilege in land to which a burden is annexed has no right to assert a claim to the privilege, and deny responsibility for the A party who acquires such a privilege acquires it subject to the conditions and burdens bound up with it, and must, if he asserts a right to the privilege, bear the burden which the contract creating the privilege brought into existence. In this instance the covenant written in the deed was an essential part of it, and the agreement to construct the fence was part of the consideration for the land."133.

The principle involved in the case just referred to does not apply to purely personal contracts of the old corporation. A contract by a railroad company not to extend its road in a certain direction does not create an obligation running with the road, but is a purely personal contract, and therefore it is not

<sup>133</sup> Midland Ry. Co. v. Fisher, 125 Ind. 19, 21 Am. St. Rep. 189.

binding upon another corporation purchasing the company's road and franchises at a foreclosure sale. 184

The same is true of a contract between a railroad company and lumber dealers to carry lumber for a specified time at specified rates. It is not binding upon a corporation which purchases the railroad and franchises. A life pass issued by a street railroad company does not bind its successor unless by agreement to recognize the same. 136

#### § 343. Liability of old corporation.

When a corporation sells its property and franchises, or they are sold under an execution, or under a decree foreclosing a mortgage thereon, the corporation is not thereby dissolved, unless there is some statutory provision to such effect, and it remains liable upon its debts and its executory contracts, and for its torts, and may be sued, notwithstanding the sale.<sup>137</sup> Whether or not the creditor may follow and subject the property in the hands of the purchaser depends upon the circumstances. The question has been considered in the section preceding.<sup>138</sup>

If there is a statutory provision under which the sale and transfer amounts to a dissolution of the corporation, 139 it cannot afterwards be sued, unless there is some provision by which its existence is continued for such a purpose. 140 But even when there is a dissolution of the old corporation, its creditors may proceed in equity to reach and subject to the payment of their claims any of its assets which have not come into the hands of a bona fide purchaser for value. 141

The old corporation is clearly not liable for any debts contracted or wrongs committed by the succeeding corporation, unless the circumstances are such as to make it liable under some principle of the law of agency.\* A railroad company,

<sup>134</sup> City of Menasha v. Milwau- Co. v. Maddox (Tex. Civ. App.) kee & Northern R. Co., 52 Wis. 31 S. W. 702.

<sup>&</sup>lt;sup>126</sup> Tawas & Bay County R. Co. v. Iosco County Circuit Judge, 44 Mich. 479.

<sup>&</sup>lt;sup>136</sup> Eddy v. Hinnant, 82 Tex. 356; Dallas Consolidated Traction Ry.

<sup>137</sup> Ante, §§ 309-311.

<sup>138</sup> Ante, § 342. 139 Ante, § 308.

<sup>140</sup> Ante, §§ 326-329, 332.

<sup>141</sup> Ante, § 328(b).

<sup>\*</sup>When a corporation permits a

for example, is not liable for personal injuries or injuries to stock or other property, caused in the operation of its road after it has been sold under a decree of foreclosure, and has thus passed out of its possession and control.142

The old corporation may, of course, be released from liability for its debts by a valid agreement between it and its creditors, as in the case of an agreement between a corporation and its creditors and another corporation, by which the latter agrees to assume the former's debts, and the creditors agree to the change of debtors. Here there is a novation, and the creditors' remedy after the agreement is against the new corporation only. 143 The creditors must be parties to the agreement in order that the old corporation may be released, for a creditor cannot be compelled to assent to a change of debtors.144

If a corporation makes an assignment for the benefit of creditors, and the creditors afterwards consent to a reorganization of the corporation, and accept its bonds or notes in satisfaction of their claims, they thereby release any rights they may have had, under the assignment or otherwise, against the property of the old corporation.145

Of course, a promise by a creditor of a corporation to look to another corporation for payment of his claim is not binding unless supported by a consideration. A promise by a corporation to pay part of its indebtedness with stock in a proposed new corporation, and the balance in cash and notes of the new corporation, is no consideration, so long as it is unperformed, for a promise by a creditor to subscribe for his proportion of the stock of the new corporation, and to accept the same, with the cash and notes, in full satisfaction of his claim, for the cor-

newly-organized corporation to absorb all its assets and do business in its name, it is liable for obligations so contracted, as it assumes to be a principal in such transactions. Davis Provision Co. v. Fowler Bros., 20 App. Div. 626, af-firmed 163 N. Y. 580.

Ala. 578.

143 See Friedenwald Co. v. Asheville Tobacco Works, 117 N. C. 544; Island City Savings Bank v. Sachtleben, 67 Tex. 420. And see ante, § 342(g).

144 See Cole v. Millerton Iron

Co., 133 N. Y. 164.

145 First Nat. Bank of Chatta-142 Western R. Co. v. Davis, 66 nooga v. Radford Trust Co. (C. C. A.) 80 Fed. 569.

poration has no power to bind the proposed new corporation, and such an agreement is revocable, therefore, at any time before actual performance. 146

#### § 344. Change of state or other bank into a national bank.

(a) In general.—Express provision is made, in the act of congress relating to national banking associations, for the reorganization of state banks into national banks. It is provided therein, in substance, that any bank incorporated by special law, or any banking institution organized under a general law of any state, may become a national banking association by the name prescribed in its organization certificate; "and in such case the articles of association and the organization certificate may be executed by a majority of the directors of the bank or banking institution; and the certificate shall declare that the owners of two-thirds of the capital stock have authorized the directors to make such certificate, and to change and convert the bank or banking institution into a national association. majority of the directors, after executing the articles of association and organization certificate, shall have power to execute all other papers, and to do whatever may be required to make its organization perfect and complete as a national association." There are other provisions not necessary to mention in this connection.147

No authority other than that conferred by the act of congress is required to enable a bank existing under a general or special state law to reorganize as a national banking association. 148

Under the act above referred to, and under the act of June 30, 1876, providing that all savings or other banks organized in the District of Columbia under any act of congress, which

<sup>146</sup> Providence Albertype Co. v. Kent & Stanley Co., 19 R. I. 561. 147 Rev. St. U. S. § 5154.

banks under this provision, see 40 Ohio St. 528; Lockwood v. v. Phoenix Bank, 34 Conn. 205;

State v. Hartford Nat. Bank, 34 Conn. 240; Thomas v. Farmers' Bank of Maryland, 46 Md. 43; As to the reorganization of state Western Reserve Bank v. McIntire; Casey v. Galli, 94 U. S. 673; State Mechanics' Nat. Bank, 9 R. I. 308. 148 Casey v. Galli, 94 U. S. 673.

shall have capital stock paid up in whole or in part, shall be subject to all the provisions of the Revised Statutes, and of all acts of congress applicable to national banking associations, so far as the same may be applicable to such savings or other banks, such banks are entitled to organize as national banks.<sup>149</sup>

The certificate of the comptroller of the currency is conclusive as to the regularity of the proceedings converting a state bank or a bank of the District of Columbia into a national bank. 150

A state law authorizing any state banking corporation to become a national banking association under the laws of the United States, and providing that it may continue to use its corporate name for the purpose of prosecuting and defending suits, etc., simply confers a privilege, and does not impair their efficiency to perform their functions as agencies of the United States government, nor conflict with the act of congress requiring national banks to have a corporate name, etc.<sup>151</sup>

(b) Effect of change from state to national bank.—It is not very clear how a banking corporation organized under state laws, owing its existence and powers to such laws, and being purely a state corporation, can properly be said to be the same corporation when it has reorganized under the national banking act, and become a federal corporation, deriving its existence and powers solely from the laws of the United States. How, in the nature of things, can a corporation existing solely under and by virtue of the laws of one sovereignty be the same as a corporation existing solely under and by virtue of the laws of another sovereignty?

However this may be in reason, it is settled, in so far as decisions can settle a question, that when a state bank is reorganized as a national bank under the act of congress, the reorganization does not change the identity of the corporation, but merely continues the same body under a different jurisdic-

<sup>149</sup> Keyser v. Hitz, 133 U. S. 138, 151 Thomas v. Farmers' Bank of Markey (D. C.) 473. Maryland, 46 Md. 43.

<sup>2</sup> Mackey (D. C.) 473. 150 Keyser v. Hitz, 2 Mackey (D. C.) 473, 133 U. S. 138.

tion, and that, as a national bank, it takes all the assets possessed by it, and becomes subject to all the liabilities incurred by it, as a state bank.<sup>152</sup> "The general scheme of the national banking act," said the New York court of appeals, "is that state banks may avail themselves of its privileges and subject themselves to its liabilities, without abandoning their corporate existence, without any change in the organization, officers, stockholders, or property, and without interruption of their pending business or contracts. All property and rights which they held before organizing as national banks are continued to be vested in them under their new status. though, in form, their property and rights as state banks, purport to be transferred to them in their new status of national banks, yet in substance there is no actual transfer from one body to another, but a continuation of the same body, under a changed jurisdiction. As between it and those who have contracted with it, it retains its identity, notwithstanding its acceptance of the privilege of organizing under the national banking act."153

--- Assets.-- It follows from this view of the act of congress that when a state bank is reorganized as a national banking association, it becomes, as a national bank, the owner of all the assets of the state bank, including choses in action. 154

152 Michigan Insurance Bank v. Eldred, 143 U.S. 293; Metropolitan Nat. Bank v. Claggett, 141 U. S. 520; Coffey v. National Bank of Missouri, 46 Mo. 140, 2 Am. Rep. 153; City Nat. Bank of Poughkeepsie v. Phelps, 97 N. Y. 44, 49 Am.

153 City Nat. Bank of Poughkeepsie v. Phelps, 97 N. Y. 44, 49 Am. Rep. 513.

In a Missouri case it was said, speaking of a change of a state bank to a national bank: "It thus passed from one jurisdiction to another; but its identity was not thereby necessarily destroyed. It remained substantially the same

The transition did not disturb the relation of either the stockholders or officers of the corporation, nor did it enlarge or diminish the assets of the institution. These all remained the same under the national as they were under the state Rep. 513; Thorp v. Wegeforth, 56 organization. The bank neither Pa. St. 82, 93 Am. Dec. 789. any of its liabilities by the change. The change was a transition, and not a new creation." Coffey v. National Bank of Missouri, 46 Mo. 140, 2 Am. Rep. 488.

154 Western Reserve Bank v. Mc-Intire, 40 Ohio St. 528; Grocers' Nat. Bank v. Clark, 48 Barb. (N. Y.) 26; and cases hereafter cited.

When a state bank, after paying institution under another name, to its president money falsely repmakes no difference that it has in form been organized as a new corporation, and that the assets have been transferred to it as if by sale and purchase.155

---Contracts-Rights of action.-The national bank succeeds to and is entitled to enforce all contracts and rights of action which have been made with or accrued to the state bank. 156 It may maintain an action on a continuing guaranty for loans. held by the state bank before the change, for loans both before and after the change. 157 And it may maintain an action to foreclose a mortgage on real estate executed to the state bank as security for a loan made upon a note, and assigned to it by the state bank on the reorganization, 158 or, it would seem, without any assignment, the identity of the corporation not being affected by the reorganization. 159

-Liabilities.-On the other hand, as a national bank it is liable for all the debts contracted, on all executory contracts made, and for all torts committed by it as a state bank. 160 is liable, as a national bank, to the holders of outstanding circulation issued by it as a state bank in accordance with state laws. 161 It is liable for a reward offered by it as a state bank for the apprehension and conviction of one who had robbed And it is liable in an action of trover to recover the value of a special deposit made with it as a state bank and con-

resented by him to have been paid 40 Ohio St. 528; Grocers' Nat. Bank to an agent to whom the bank was indebted, was reorganized into a national bank, it was held that the sie v. Phelps, 97 N. Y. 44, 49 Am. national bank, after a suit against it by the agent, and recovery of a judgment, could maintain an action against the president in its own name for money had and received under a statute allowing the assignee of a chose in action to sue in his own name. Atlantic Nat. Bank v. Harris, 118 Mass. 147.

155 Western Reserve Bank v. Mc-Intire. 40 Ohio St. 528.

156 Michigan Insurance Bank v. Eldred, 143 U. S. 293; City Nat. Bank of Poughkeepsie v. Phelps, 97 N. Y. 44, 49 Am. Rep. 513; Western Reserve Bank v. McIntire, Crawford County, 69 Pa. St. 426.

v. Clark, 48 Barb. (N. Y.) 26.

157 City Nat. Bank of Poughkeep-

158 Scofield v. State Nat. Bank of Lincoln, 9 Neb. 316, 31 Am. Rep.

159 See supra, this section. <sup>160</sup> Metropolitan Nat. Bank v. Claggett, 141 U. S. 520; Coffey v. National Bank of Missouri, 46 Mo. 140, 2 Am. Rep. 488; Thorp v. Wegefarth, 56 Pa. St. 82, 93 Am. Dec. 789; Kelsey v. National Bank of Crawford County, 69 Pa. St. 426.

<sup>161</sup> Metropolitan Nat. Bank v. Claggett, 141 U. S. 520.

162 Kelsey v. National Bank of

verted, whether the conversion was before or after its reorganization as a national bank.<sup>163</sup>

Bonus exacted by state.—A national bank is not liable to the state in which it is organized for a bonus exacted by the state, for its franchises and privileges, from the state bank from which it was reorganized, for, as a national bank, it does not derive its franchises and privileges from the state.<sup>164</sup>

# § 345. Reorganization agreements, and rights of bondholders, stockholders, and creditors generally.

The reorganization of a corporation may be brought about in various ways, and under varying circumstances. It may be brought about in pursuance of an agreement of all the parties, without any foreclosure, or by transfer of the property to a new corporation, or by purchasing the property at a foreclosure sale, and organizing a new corporation to take the same and continue the business. In some states, elaborate provisions for reorganization of corporations have been made by statute. Many late decisions are to be found in the reports involving the construction of reorganization agreements, but it is obviously impossible, in a work of this size and scope, to review or refer to all of them. All that can be done is to treat the subject in a very general way, showing the principles of law which apply to reorganizations and reorganization agreements, and the rights of stockholders, bondholders, and general creditors in case of reorganization.

(a) Reorganization without foreclosure—(1) In general.—Reorganization of a corporation which has issued bonds secured by a mortgage, and which has become embarrassed and unable to pay the interest, is sometimes effected by an agreement with the stockholders and bondholders, under which the stock and bonds, or bonds only, of the company are readjusted, so as to enable the company to continue business without a foreclosure

<sup>&</sup>lt;sup>163</sup> Coffey v. National Bank of <sup>164</sup> State v. National Bank of Missouri, 46 Mo. 140, 2 Am. Rep. Baltimore, 33 Md. 75. 488.

of the mortgages on its property, the stockholders perhaps taking new stock, and the bondholders surrendering their bonds. and taking new bonds differing from the old bonds as to amount, rate of interest, or priority, etc. 165 Such a reorganization is voluntary, and requires the assent of all the parties interested. If any stockholder or bondholder refuses to come into the arrangement, he cannot be compelled to do so. may insist upon his rights as a stockholder or bondholder, and prevent any reorganization which will affect the rights secured to him by his contract with the company. 166 A bondholder has a right to refuse to come into the agreement, and to insist upon payment of his bonds, or upon a foreclosure of the mortgage by which they are secured, and if the stockholders and other bondholders proceed with a reorganization without his consent, he will not be bound thereby. 167

It has been held that if a scheme of reorganization without foreclosure is authorized by the court, in a suit to which the trustee for the bondholders is a party, and a bondholder refuses to go into it, the amount due him on his bonds may be paid or tendered, and, if he refuses to accept payment, the court may compel him to surrender his bonds.168

## - (2) Effect of agreement and reorganization.—Any party,

93 Pa. St. 95; Gilfillin v. Union Ziegler (C. C. A.) 99 Fed. 114. Canal Co., 109 U. S. 401; Pollitz v. 210; Mowry v. Farmers' Loan & Western Ry. Co., 55 How. Pr. (N. Trust Co. (C. C. A.) 76 Fed. 38; Park v. Grant Locomotive Works, 40 N. J. Eq. 114.

Y. 644.

A court of equity will not, at Mere silence of a bondholder the suit of a corporation, compel when a plan of reorganization is minority bondholders to assent published is no ground for implytts minority bondholders to assent to a reorganization scheme by ing his consent thereto, where, as which they are required to scale their bonds, accepting in lieu thereof new bonds for a smaller amount, without additional security; the benefits of the scheme, if any, inuring solely to the stockholders, published is no ground for implying his consent thereto, where, as one of the directors of a corporation, he has voted against the same. Philadelphia & Reading R. Co. v. Love, 125 Pa. St. 488.

165 Union Canal Co. v. Gilfillin, Lake Street Elevated R. Co. v. 167 Hollister v. Stewart, 111 N. Farmers' Loan & Trust Co., 53 Fed. Y. 644; Taylor v. Atlantic & Great Y.) 275; Reinach v. Meyer, 55 ark v. Grant Locomotive Works, How. Pr. (N. Y.) 283; Bill v. New Albany, etc., Ry. Co., 2 Biss. 390, Fed. Cas. No. 1,407; Philadelphia & Reading R. Co. v. Love, 125 Pa. St. 488.

whether a stockholder, bondholder, or other creditor, or the corporation itself, who enters into a valid agreement for the purpose of reorganization, is bound thereby, and cannot repudiate the same, and insist upon his original rights in violation of its terms, either before or after the agreement has been carried out.169 Thus, if a corporation makes an assignment for the benefit of creditors, and the creditors afterwards consent to a reorganization, and accept the notes or bonds of the reorganized company in satisfaction of their claims, they release any rights which they may have had under the assignment or otherwise against the property of the corporation. 170

In a proper case, a valid reorganization agreement will be specifically enforced.171

(3) Consideration for agreement.—An agreement for reorganization, like any other contract, is not binding unless the promises of the parties are supported by a consideration.\* Or-

First Nat. Bank of Chattanooga v. Radford Trust Co. (C. C. A.) 80 Fed. 569. See Glens Falls Paper Mill Co. v. Trask, 29 App. Div. 449, affirmed 164 N. Y. 604.

If the holders of first mortgage bonds enter into an agreement by which they waive their lien, and agree to take second mortgage bonds instead, and the first mortgage is discharged, their rights as first mortgage bondholders are gone. If the corporation fails to issue to them second mortgage bonds, as required by the agreement, they will be entitled to share as second mortgage bondholders in the proceeds of a foreclosure sale, but they are not thereby restored to their former position as first mortgage bondholders. Fidelity Insurance, Trust & Safe Deposit Co. v. Shenandoah Valley R. Co., 33 W. Va. 761. <sup>170</sup> First Nat. Bank of Chatta-

nooga v. Radford Trust Co. (C. C. A.) 80 Fed. 569.

169 Dester v. Ross, 85 Mich. 370; the debts of the old company, and creditors of the latter accepted bonds of the new company as a full satisfaction of their claims, it was held that they lost any lien or priority they may have had, imposed by the charter of the new company, what they thus received being substantially different in amount and security from what they were entitled to thereunder. Commonwealth of Virginia v. State, 32 Md. 501.

171 Dester v. Ross, 85 Mich. 370. Of course the agreement must be sufficiently definite to be capable of being specifically enforced. See Ballou v. March, 133 Pa. St. 64.

\* The fact that the creditors of an insolvent corporation were not made parties to an agreement included in a plan for its reorganization, binding the stockholders to give their notes to the corporation to the amount of their respective holdings of stock, to be collected in case of "a deficiency of assets," and providing that payment there-Where a corporation assigned of should pro tanto discharge the its charter to a new corporation, stockholders' statutory liability exin consideration of its payment of isting at the date of the agreement, dinarily it is a case of mutual promises, in which the promise of each party is supported by the promises of the others, but the promise of one of the parties may for some reason be unenforceable, and in such a case it would not be a consideration for the promise of the other. Thus, a promise by a corporation to pay part of its indebtedness with stock in a proposed new corporation, and the balance in cash and notes or bonds of the new corporation, is no consideration, so long as it is unperformed, for promises by creditors to subscribe for their proportion of the stock of the new corporation, and to accept the same, with the cash and notes or bonds, in full satisfaction of their claims, for the corporation has no power to bind the proposed new corporation. Such an agreement, therefore, is revocable by either party at any time before actual performance. 172

(b) Transfer of property to a new corporation.—A reorganization is sometimes effected, without foreclosure of a mortgage. by transferring all the property of the corporation to a new corporation, either by absolute sale or by lease. Such a transaction may be ultra vires, or it may not, according to the circumstances, as explained in a former chapter. 173 Whether it is within the power of a majority of the stockholders to authorize such a transfer against the dissent of the minority will

106 Wis. 34.

son v. Gross, 106 Wis. 34.

Where the holder of receiver's certificates of an insolvent corporation, the validity of which is being contested in an action by the

does not affect the validity of the bondholders of the company, agrees, agreement. Thompson v. Gross, in consideration that the certificates shall be recognized as valid, Such agreement is not void on and a decree entered to that effect, the part of the stockholders for to advance money for the purpose want of consideration, on the of reorganizing the company, takground that the corporation can- ing in return therefor, and for his not release their statutory liability certificates, first mortgage bonds, to creditors, since payments under the bondholders to receive second the agreement constitute a trust mortgage bonds, the performance fund in the hands of the corpora- of the agreement by the bondholdtion, in which creditors cannot par- ers by procuring the decree conticipate except by releasing pro stitutes a sufficient consideration tanto their rights against the stock- for the agreement. Cox v. Stokes, holders under the statute. Thomp- 156 N. Y. 491, reversing 78 Hun,

172 Providence Albertype Co. v. Kent & Stanley Co., 19 R. I. 561.

173 Ante, §§ 160-163.

Se considered in a subsequent chapter. 174 The transfer, of course, cannot deprive nonassenting bondholders or others having a lien upon the property of the right to enforce the same: nor can it prevent unsecured creditors from following the property into the hands of the transferee. 175 They cannot be compelled to accept a change of debtors against their will. 176

Such a reorganization will not be allowed to stand if a fraud has been perpetrated by some of the stockholders upon the others, or by officers of the corporation upon stockholders. When such a transfer has been agreed upon, it must be carried out in good faith, and in the interest of all the parties. If a majority of the stockholders of a corporation authorize a sale of its property for the purpose of a reorganization, they cannot themselves, directly or indirectly, purchase at the sale to the exclusion or prejudice of other stockholders. 177 Nor can any one or more of the directors or other managing officers of the corporation purchase at such a sale. If they do so, the sale is voidable at the suit of any stockholder. 178

In disposing of the property of a corporation and winding up its affairs after expiration of its charter, under a statute continuing its existence for such purpose, neither the directors nor a majority of the stockholders can sell the property to a new corporation, of which they are directors and stockholders, on an arbitrary estimate of its value made by themselves, and compel a dissenting minority of the stockholders either to take shares in the new corporation in exchange for their shares in the old, or to accept payment of their proportion in money on the basis of the estimated valuation. 179

<sup>174</sup> Post, chapter xxiv.

<sup>175</sup> Ante, § 342(i).

<sup>176</sup> Grenell v. Detroit Gas Co., 112 Mich. 70.

<sup>177</sup> Meeker v. Winthrop Iron Co., 17 Fed. 48; Mason v. Pewabic Mining Co., 133 U. S. 50; Farmers' Mining Co., 133 U. S. 50; Farmers' Arkansas Mechanical & Agricult-Loan & Trust Co. v. New York & ural Co., 38 Ark. 17. See, also, Northern Ry. Co., 150 N. Y. 410, infra, this section, (c) (7). 55 Am. St. Rep. 689; Chicago Hansom Cab Co. v. Yerkes, 141 Ill. 133 U. S. 50. See ante, § 332(e). 55 Am. St. Rep. 689; Chicago Han-

<sup>320.</sup> And see infra, this section, (c)(6).

<sup>178</sup> See Hoffman Steam Coal Co. v. Cumberland Coal & Iron Co., 16 Md. 456; Cumberland Coal & Iron Co. v. Sherman, 30 Barb. (N. Y.) 553; Jones, McDowell & Co. v.

(c) Foreclosure and sale under mortgage or deed of trust and other judicial sales—(1) In general.—Corporations are also frequently reorganized by procuring a foreclosure and sale under the mortgage or deed of trust given by it to secure its bonds. purchasing its property and franchises at the sale, and causing the same to be transferred to another corporation organized for the purpose by the stockholders or bondholders, or both, or by some of them. When a railroad company or other corporation, which has issued bonds and given a mortgage or deed of trust to secure the same, becomes embarrassed and unable to pay the interest or principal, it is often advisable, and perfectly legal, for the bondholders, or a part of them, to formulate some scheme for reorganization of the corporation after a sale of the property under a decree foreclosing the mortgage or deed of trust, or under a power of sale given in the same. They may enter into an agreement for this purpose, appoint a committee or other agent to represent them, to purchase the property at the foreclosure sale for their benefit, to form a new corporation, and to transfer the property to it in return for stock or bonds, or both, to be issued to them by it in accordance with the agreement. Such an agreement, and the purchase in pursuance thereof, are not only legal, but are regarded with favor by the law.180

The right of the bondholders to thus purchase for the purpose of reorganization is not limited to foreclosure sales under a decree of the court. They may purchase at a sale by the trustee under a power of sale given in the mortgage or deed of trust.181

180 See Shaw v. Little Rock & 302; Mackintosh v. Flint & Pere Ft. Smith R. Co., 100 U. S. 605; Marquette R. Co., 34 Fed. 582; Robinson v. Philadelphia & R. R. Gates v. Boston & New York Air Co., 28 Fed. 340; Easton v. German American Bank, 127 U. S. New York & New England R. Co., 532; Farmers' Loan & Trust Co. v. 129 Mass. 170.

Green Bay & Minnesota R. Co., 6

Fred 100; Plett v. Philadelphia & 181 Easton v. German American Fed. 100; Platt v. Philadelphia & Reading R. Co., 65 Fed. 872; Kropholler v. St. Paul, Minneapolis & And see Child v. New York & M. Ry. Co., 1 McCrary, 299, 2 Fed. New England R. Co., 129 Mass. 170.

181 Easton v. German American Bank, 127 U. S. 532.

And see Child v. New York &

As we have seen, the result of a valid foreclosure sale, in the absence of statutory provision to the contrary, and provided there is no fraud, is to transfer the property to the purchaser free from any claims on account of the liabilities of the old corporation not secured by prior lien, except such as may be expressly assumed; and the only rights of creditors of the old corporation, not secured by prior lien, are the right to participate in the proceeds of the sale, according to their priorities. and such rights, if any, as may be given them by the reorganization agreement.182

-(2) Rights as between bondholders.—When two or more persons have a common interest in a security, equity will not allow one of them to appropriate it exclusively to himself, or to impair its worth to the others. Community of interest involves mutual obligation. It has been held, therefore, that when a corporation has issued bonds secured by a mortgage of its property, one of the bondholders, although he may have a right to make use of the mortgage to enforce payment of the bonds which he holds, has no right to employ it as an instrument by which he may become the owner of the property mortgaged at the lowest price at which it can be obtained, leaving the bonds of the other holders unpaid. His duty, if he makes use of the mortgage at all, is to make it productive of the most that can be obtained for all who are interested in it; and if he seeks to make a profit out of it at the expense of those whose rights in it are the same as his own, he is guilty of a fraud. 183

cases there cited.

183 Jackson v. Ludeling, 21 Wall. (U.S.) 616.

See, also, Florida v. Anderson, Where some of the bondholders 90 U. S. 667; Sahlgard v. Kennedy, 2 Fed. 295; Duncan v. Mobile & cure a foreclosure, and purchase

182 See ante, § 342(e), (d), and part of the bondholders to give them an advantage over the others is a fraud upon the latter, and is therefore illegal and void. Bliss v. Matteson, 45 N. Y. 22.

Ohio R. Co., 3 Woods, 597, Fed. the property for the purpose of re-Cas. No. 4,139 (where, prior to a organization, to the exclusion or foreclosure sale, the court ordered, injury of other bondholders, the on application of minority bond-holders, that they be permitted to participate in the reorganization). claim or lien upon the property. Any special agreement with a Richter v. Jerome, 123 U. S. 233.

This principle does not apply, however, where there is no attempt to take an unfair advantage of other bondholders, particularly when all are given an opportunity to come into the reorganization arrangement on equal terms. Those who refuse to come in cannot complain that the others who have purchased at a foreclosure sale under the mortgage have made a large profit, or claim any share therein. 184 It has been held, therefore, that the conduct of a railroad reorganization committee in fairly and openly seeking to obtain the co-operation of all the bondholders in buying in the railroad at a foreclosure sale, and organizing a new company, although it results in a large profit to the assenting bondholders, does not make them trustees for nonassenting bondholders, or give the latter any right other than to share in their proportion of the proceeds of the sale applicable to the bonds. "When a sale of mortgaged railroad property is decreed," said the court, "an association of bondholders for the protection of their mutual interest is a necessity, and the appointment of a committee to act for them is advisable and customary. Those charged under the terms of such association with the duty of acting must employ counsel and be responsible for expenses and costs. That one of the terms of being admitted to such an association should be the deposit of the bonds to be protected is surely most reasonable. If notice of the fullest kind possible is given to all bondholders, and all are invited to come into the association upon the same terms, and the privilege is not withdrawn until there is a really valid reason for doing so, there can be no just complaint by those whose inaction has left them outside that they do not share in the benefits of those who are inside the association, and have taken the risks of its success or failure."185

Even where some of the bondholders have no notice of a foreclosure sale, at which the property is purchased by a part

Co. (C. C. A.) 78 Fed. 49, affirm—Co., 1 McCrary, 466, 3 Fed. 177. ing 71 Fed. 53, and distinguishing Jackson v. Ludeling, 21 Wall. 616;

<sup>184</sup> Bound v. South Carolina R. Wetmore v. St. Paul & Pacific R.

<sup>185</sup> Bound v. South Carolina R.

of the bondholders for the purpose of reorganization, they cannot sue to set the sale aside, in the absence of fraud. 186

A mortgage or deed of trust by a corporation frequently contains a provision for reorganization in case of foreclosure, and it may be such as to give a majority of the bondholders the power to bind the minority as to the scheme or plan of reorganization.<sup>187</sup>

- —(3) Rights of second-mortgage bondholders.—The holders of second mortgage bonds of a corporation have a right to insist that a foreclosure sale under the first mortgage shall be made fairly, and without any collusion among the parties in interest which may result in a sacrifice of the property; but they cannot, in the absence of fraud, prevent the first mortgage bondholders from purchasing at the sale under an agreement for reorganization, or sue to set the sale aside, or claim any right to participate in the reorganization, unless they have rights under the agreement.<sup>188</sup>
- —(4) Who may purchase at foreclosure sale—In general.—In the absence of statutory restrictions, any person may purchase the property of a corporation at a foreclosure sale, provided his relation to the parties in interest, and the circumstances attending the purchase, are not such as to make the purchase a breach of trust. There is nothing to prevent the bondholders from purchasing, or a part of them, provided there is no fraud upon the others. They may appoint a person or committee to purchase for them, and this is the usual course. The attorney for the corporation may purchase for the bondholders, if authorized by them.

Co. (C. C. A.) 78 Fed. 49, affirming 71 Fed. 53.

186 Gates v. Boston & New York Air Line R. Co., 53 Conn. 333. See, also, Terbell v. Lee, 40 Fed. 40; Easton v. German American Bank, 127 U. S. 532.

187 Sage v. Central R. Co., 99 U.S. 334.

<sup>188</sup> See Robinson v. Iron Ry. Co., 135 U. S. 522.

189 See the cases cited under the preceding paragraphs.

190 Allen v. Gillette, 127 U.S. 589; Pacific R. Co. v. Ketchum, 101 U. S. 289; James v. Cowing, 82 N. Y. 449; Zebley v. Farmers' Loan & Trust Co., 129 N. Y. 461; and other cases cited under the preceding paragraphs, and the paragraphs following.

191 Pacific R. Co. v. Ketchum, 101
 U. S. 289.

The right of the trustee in the mortgage or deed of trust to purchase for the bondholders or for himself, or to be interested in the purchase, and the right of officers of the corporation or stockholders to purchase, are considered in the paragraphs following.

(5) Purchase and transfer by trustee.—The trustee in a mortgage or deed of trust by a corporation to secure the payment of its bonds occupies a fiduciary relation towards the corporation and the bondholders, and he certainly cannot purchase for himself at his sale under the mortgage or deed, or be-interested in the purchase. If he does so, he may be compelled to account for any profit, or the sale may be set aside.192 unless relief is barred on the ground of laches or acqui-Nor can the agent of the trustee in possession and escence. 193 control of the property purchase at the sale. 194

And since the trustee represents or occupies a fiduciary relation towards the corporation, as well as the bondholders, it has been held that he cannot purchase even for the benefit of the bondholders, 195 unless the sale is brought about by other interests or parties, 196 or the mortgage or deed of trust, as is sometimes the case, expressly authorizes him to bid in the property for the benefit of the bondholders, 197 or he is directed

192 People v. Merchants' Bank, v. Farmers' Loan & Trust Co., 49 35 Hun (N. Y.) 97; Racine & Mis-sissippi R. Co. v. Farmers' Loan & Trust Co., 49 Ill. 331, 95 Am. Dec. 595. V. Farmers' Loan & Trust Co., 49 People State Wissington Alexandria v. Farmers' Loan & Trust Co., 49 Dec. 595; Washington, Alexandria & G. R. Co. v. Alexandria & Washington R. Co., 19 Grat. (Va.) 592, 100 Am. Dec. 710.

Where a bank holding bonds of a corporation, and whose cashier was trustee in the mortgage securing the same, purchased at the foreclosure sale under the mort-gage, it was held that the other bondholders could compel it to account for the profits. People v. Merchants' Bank, 35 Hun (N. Y.)

193 See Hoyt v. Latham, 143 U.

194 Racine & Mississippi R. Co. Trust Co., 163 N. Y. 461.

Ill. 331, 95 Am. Dec. 595; Washington, Alexandria & G. R. Co. v. Alexandria & Washington R. Co., 19 Grat. (Va.) 592, 100 Am. Dec. 710. See, also, James v. Milwau-kee & Minnesota R. Co., 6 Wall. (U.S.) 752.

Laches may bar the right to set the sale aside. Kitchen v. St. Louis, Kansas City & N. Ry. Co., 69 Mo. 224.

196 Allen v. Gillette, 127 U. S.

197 James v. Cowing, 82 N. Y. 449; Zebley v. Farmers' Loan &

or authorized to do so, as he may be, by the decree of the court directing the sale, 198 or by a statute. 199 Where the trustee does buy in the property at his own sale, he is not in a position to object that he had no right to do so.200

In any case, when the trustee bids in the property, and transfers the same to a new corporation, he must do so for the benefit of all the bondholders whom he represents, and, if he disregards the rights of a bondholder, he is liable to him for the loss sustained,<sup>201</sup> in the absence of laches.<sup>202</sup> mortgage or deed of trust requires him to organize a new corporation, and transfer the property to it, he is under a duty to do so, and he has no right to sell the property to another corporation, instead of the reorganized corporation, even with the consent of a majority of the bondholders. he does so, a dissenting bondholder may hold him liable for the value of his bonds.<sup>203</sup>  $\Lambda$  bondholder cannot complain of a transfer by the trustee to a new corporation, to which he has assented 204

If the trustee, after purchasing for the benefit of the bondholders, joins with one or more of the bondholders, to the exclusion of others, in forming a new corporation and transferring the property to it, he and the other bondholders who joined with him may be compelled to account for profits to the bondholders excluded,205 or to account for their share of the proceeds of the sale, or of the value of the property, 206 or they may sue to set the sale aside.207

The trustee has no right to make any secret profit at the

198 Sage v. Central R. Co., 99 U. S. 334; Rogers v. Wheeler, 43 N. Y. 598. Compare Sanxey v. Iowa City Glass Co., 63 Iowa, 707.

189 Barnes v. Chicago, Milwau-kee & St. P. R. Co., 8 Biss. 514, Fed. Cas. No. 1,016.

200 Barnes v. Chicago, Milwaukee & St. P. R. Co., 8 Biss. 514, Fed. Cas. No. 1,016.

<sup>201</sup> James v. Cowing, 82 N. Y. 449; Zebley v. Farmers' Loan &

Trust Co., 139 N. Y. 461; Riker v. Alsop, 27 Fed. 251, 155 U.S. 448. 202 Alsop v. Riker, 155 U. S. 448.

203 James v. Cowing, 82 N. Y.

204 Butterfield v. Cowing, 112 N. Y. 486.

205 Cushman v. Bonfield, 139 Ill.

206 Zebley v. Farmers' Loan & Trust Co., 139 N. Y. 461.
207 Sahlgard v. Kennedy, 1 Mc-

Crary, 291, 2 Fed. 295.

expense, either of the bondholders, or of the corporation, for he represents both. Where a trustee in a railroad mortgage. in possession of the property as such, made a profit by buying up some of the bonds, he was held accountable therefor to the company.208

- -(6) Purchase by or for stockholders.—A majority of the stockholders of a corporation cannot combine to procure a foreclosure and sale, and a reorganization, to the prejudice of the other stockholders, for the majority occupy a fiduciary relation towards the minority, and it is their duty to see that the best possible price is obtained at the sale. Collusion on their part will entitle an injured stockholder to sue to set the sale aside.<sup>209</sup> A majority of the stockholders, however, may purchase at the sale, by themselves or through an agent, and reorganize, if they do so in good faith, and without taking any undue advantage.210
- ---(7) Purchase by directors or other officers.—The managers or directors and other officers of a corporation are in a sense trustees both for its stockholders and creditors, and therefore they have no right, although they may also be creditors, to enter into any combination, the object of which is to divest the company of its property, and obtain it for themselves, directly or indirectly, at a sacrifice. They have no right to obtain any profit or advantage for themselves at the expense of the company or its stockholders, or even of its bondholders. If the company is embarrassed, and there is any necessity to sell its property, it is their duty, to the extent of their power, to secure, for all those whose interests are in their charge, the

N. H. 397.

200 See Ribon v. Railroad Cos., 16 Wall. (U. S.) 446; Farmers' Loan & Trust Co. v. New York & Northern Ry. Co., 150 N. Y. 410, 55 Am. St. Rep. 689; Mason v. Pewalic Mining Co., 133 U. S. 50; Hanley v. Balch, 94 Mich. 315. See, also, post, chapter xxiv.

208 Ashmelot R. Co. v. Elliot, 57 the consenting stockholders must be made parties, or the bill will be demurrable. Ribon v. Railroad Cos., 16 Wall. (U. S.) 446.

210 Pewabic Mining Co. v. Mason, 145 U. S. 349; Carter v. Ford Plate Glass Co., 85 Ind. 180; Price v. Holcomb, 89 Iowa, 123; Wilson v. Proprietors of Central Bridge, 9 R. I. 590; Olmstead v. Distilling & Cattle Feeding Co., 73 Fed. 44. To such a suit, the trustees and See post, chapter xxiv.

highest possible price which can be obtained for it. lows that, in equity, they will not be permitted to retain any profit or advantage which they may make by disregard or violation of this duty.211

This principle was applied in the supreme court of the United States, in a leading case, where the managers and officers of an embarrassed railroad company, holding a small portion of its bonds, of which a much greater portion was held by nonresidents, obtained an order of sale under a mortgage to secure the bonds, and proceeded in a hasty and rather secret way to sell the road, and to buy it in for themselves at a price much below its value, the conditions of the sale being made such as to render it difficult for persons generally to purchase, and the whole proceeding of sale being attended also with evidences of gross disregard of the interests of the bondholders generally, and of the stockholders. Under these circumstances, the sale was set aside at the suit of the other bondholders.212

This doctrine, however, does not absolutely prohibit directors or other officers of a corporation from purchasing at a foreclosure sale of its property brought about by others than themselves, or from being interested in such a purchase, if the transaction is free from fraud, and the property is not sold at a sacrifice by reason of their interest in the purchase.213

(U. S.) 616. And see post, chapter Co., 38 Ark. 17. xxiv.

<sup>212</sup> Jackson v. Ludeling, 21 Wall. (U.S.) 616.

See, also, Harts v. Brown, 77 Ill. 226; Hope v. Valley City Salt Co., 25 W. Va. 789; Allen v. Jackson, 122 Ill. 567; Raleigh v. Fitzpatrick, 43 N. J. Eq. 501; Wilkinson v. Bauerle, 41 N. J. Eq. 635; Munson v. Syracuse, Geneva & C. Ry. Co., 29 Hun (N. Y.) 76, 103 N. Y. 58; Covington & Lexington R. Co. v. Bowler's Heirs, 9 Bush (Ky.) 468; Fed. 875; Saltmarsh v. Spaulding, Jones, McDowell & Co. v. Arkan- 147 Mass. 224; Foster v. Belcher's

211 Jackson v. Ludeling, 21 Wall. sas Mechanical & Agricultural

Laches may bar any right to relief. Twin Lick Oil Co. v. Marbury, 91 U. S. 587; Burgess v. St. Louis County R. Co., 99 Mo. 496. 213 McKittrick v. Arkansas Cen tral Ry. Co., 152 U. S. 473. See, also, Credit Co. v. Arkansas Central R. Co., 15 Fed. 46; Harpending v. Munson, 91 N. Y. 650; Inglehart v. Thousand Island Hotel Co., 109 N. Y. 454; Hayden v. Official Hotel Red-Book & Directory Co., 42

- ---(8) Rights of unsecured creditors.—The only right which the unsecured creditors have against a corporation, which can interfere with a reorganization, is the right to have all the assets of the corporation applied in payment of their claims, after the satisfaction of debts secured by lien thereon. It follows that when the property of a corporation is about to be sold on foreclosure of a mortgage thereon, an agreement between the bondholders, or bondholders and stockholders, to unite in purchasing the property at the sale, and in organizing a new corporation to take the same, is not a fraud upon the unsecured creditors of the corporation, so as to entitle them to enforce their claims against the new corporation.214
- ---(9) Payment or benefit to stockholders.--Any agreement that the stockholders of a corporation, whose property is to be sold under a mortgage, shall share in the proceeds of the sale, for the purpose of preventing them from resisting the foreclosure, is a fraud upon the general creditors of the corporation, and is void.<sup>215</sup> But the stockholders of a corporation commit no fraud against creditors by becoming stockholders in the new corporation by an arrangement entered into after the foreclosure, 216 or by purchasing stock therein, and paying full value therefor, although it may be less than par.217

Sugar Refining Co., 118 Mo. 238; Hill v. Nisbet, 100 Ind. 341; Lucas v. Friant, 111 Mich. 426; College Park Electric Belt Line v. Ide, 15 Tex. Civ. App. 273; post, chapter xxiv. And see Osborne's Adm'x v. Monks (Ky.) 21 S. W. 101.

Acts of the president and trustees of a corporation, without fraudulent intent, and after reasonable notice to stockholders, whereby a reorganization is promoted which preserves from exof the interests of assenting stockholders, are not fraudulent as to the exchange for their stock, are given original organization, although a stock in the new organization, large personal profit accrues there—where they pay in cash for each large personal profit accrues therefrom to the president, who is the share an amount greater than its principal promoter of the reormarket value. Paton v. Northern ganization. Symmes v. Union Pacific R. Co., 85 Fed. 838.

Trust Co. of New York, 60 Fed.

214 Pennsylvania Transportation Co.'s Appeal, 101 Pa. St. 576. And see ante, § 342(a)-(c).

215 Chicago, Rock Island & Pac. R. Co. v. Howard, 7 Wall. (U. S.)

216 Stewart's Appeal, 72 Pa. St. 291.

217 Ferguson v. Ann Arbor R. Co., 17 App. Div. (N. Y.) 336.

Reorganization of an insolvent tinguishment by foreclosure a part corporation is not a fraud upon creditors because stockholders, in

A plan for the reorganization of an insolvent corporation, which gives stockholders an interest in the new organization upon agreed terms, but does not include general creditors, or tender them an opportunity to join therein, is not invalid as to general creditors, unless it is such as to give stockholders that which should go to creditors, or to otherwise defraud creditors.218

(d) Construction of reorganization agreements.—Reorganization agreements frequently come before the courts for construction, and there are many decisions in the reports in which particular agreements have been construed. They are to be construed, of course, in accordance with the same rules which govern in the construction of any other contract. The intention of the parties is to be ascertained and given effect. Some of the decisions in which such agreements have been construed are referred to in the note below.219

Co., 85 Fed. 838.

of the new company, to be delivered to them within six months after "the date of the foreclosure sale," and the property was bid in by one of the assignees, and the sale confirmed, but the time for compliance with its terms was extended by the court, and the terms of the sale were finally complied with, and a conveyance decreed, it was held that the words above quoted referred to the time of completing the sale, and not to the time of bidding in the property, or of the confirmation. Houston,

218 Paton v. Northern Pacific R. holders of bonds issued by a coro., 85 Fed. 838. poration which formerly owned where, after a decree of the land, and secured by a mortforeclosure against a railroad com- gage thereon, the land having pany, the judgment creditors en-tered into an agreement for reor-bondholders in satisfaction of the ganization, assigning their judg-bonds, and having been conveyed ments to the reorganizers in con-sideration of first mortgage bonds of the new company, to be deliv-to the bondholders, see Rogers v. New York & Texas Land Co., 134 N. Y. 197.

For other cases involving the construction and effect of reorganization agreements, see Dutenhofer v. Adirondack Ry. Co., 60 Hun (N. Y.) 578; White v. Wood, 129 N. Y. 527, reversing 59 Hun, 619; Gernsheim v. Central Trust Co., 61 Hun (N. Y.) 625; Carpenter v. Catlin, 44 Barb. (N. Y.) 75; Thornton v. Wabash Ry. Co., 81 N. Y. 462; Gernsheim v. Olcott, 56 Hun (N. Y.) 644; Dow v. Iowa Central East & West Texas Ry. Co. v. Kel- Ry. Co., 144 N. Y. 426, 70 Hun, 186; As to the rights of holders of 144 N. Y. 655; Vose v. Cowdrey, 49 scrip issued by a corporation formed for the purpose of taking and tional R. Co., 11 App. Div. (N. holding land for the benefit of the Y.) 28; Glens Falls Paper Mill

(e) Powers of reorganization committee—Notice to committee.— A reorganization committee is the agent of the bondholders or other promoters of the reorganization, and its powers depend, of

course, upon the authority which has been expressly or impliedly conferred upon them.\* Generally the powers conferred are very broad.

Where a reorganization committee is broadly authorized to procure the sale of a railroad, to compound claims against the company, and pledge the bonds deposited with it, it has authority to agree with the holders of apparent claims against the company for an assignment thereof, and to pledge the bonds in its hands to secure the sums promised to be paid for such assignment, and the holders of the claims, if they

Co. v. Trask, 29 App. Div. 449, 164 156 N. Y. 491, reversing 78 Hun. N. Y. 604; Kildare Lumber Co. v. National Bank of Commerce, 30 U. S. App. 762, 69 Fed. 2; Davidson v. Mexican National R. Co., 58 Fed. 653; Hancock v. Toledo, Peoria & Warsaw R. Co., 9 Fed. 738; Matthews v. Murchison, 15 Fed. 691; Carey v. Houston & Texas Central Ry. Co., 45 Fed. 438; Meddaugh v. Wilson, 151 U. S. 333; Grant v. Pearce, 16 Ky. Law Rep. 204; Hitchcock v. Midland R. Co., 33 N. J. Eq. 86; Glymont Improvement & Excursion Co. v. Toler, 80 Md. 278; Keating v. McCutchen, 14 Tex. Civ. App. 150; Gresham v. Island City Savings Bank, 2 Tex. Civ.

\*As to the powers, duties, and liabilities of a reorganization committee, see, also, Central Trust Co. v. Carter (C. C. A.) 78 Fed. 225; Bound v. South Carolina Ry. Co., 71 Fed. 53, (C. C. A.) 78 Fed. 49.

As to the discretion of a reorganization committee as to the use, disposition, and distribution of reserved securities of the new corporation, and interference therewith by a court of equity at the suit of a stockholder, see Venner v. Fitzgerald, 91 Fed. 335.

tion committee unless they are aution, see Gerding v. Funk, 48 App. thorized to do so. Cox v. Stokes, Div. (N. Y.) 603.

As to ratification by one of the bondholders of a modification of a reorganization agreement unlawfully made by the reorganization committee in favor of one of the parties thereto, and to the prejudice of the bondholders, see Cox v. Stokes, 156 N. Y. 491, reversing 78 Hun, 331.

Bondholders of a corporation who have exchanged their bonds for those of a reorganized company, which, by the reorganization agreement, were to be made a first lien on the property of the company, have a right to enforce such agreement, and to insist upon the retention by the reorganization committee of all securities placed in its hands to secure the taking up of prior liens until their extinguishment is assured; and an arrangement by which such liens are to be paid off or extended at the option of the holders does not meet the requirements of the agreement. Peoria & E. Ry. Co. v. Coster, 97 Fed.

As to the personal liability of the chairman of a reorganization com-A reorganization agreement can-mittee for services of a person emnot be modified by the reorganiza- ployed by him in the reorganizaare not paid as agreed, are entitled to be paid out of the proceeds of the foreclosure sale applicable to the bonds.<sup>220</sup>

Where the committee is given authority to arrange the details of the reorganization, it may determine and provide how and when the bonds to be issued by the company shall be payable.<sup>221</sup> And it may issue only a portion of the authorized stock, leaving the balance unissued, instead of issuing the whole, 222

- -Notice to committee.-Where a reorganization agreement makes the reorganization committee the agent of the signers of the agreement, notice to the committee of matters pertaining to the reorganization is equivalent to notice to the signers. 223
- (f) Turning in bonds in payment for property.-When the bondholders purchase the property of a corporation at a foreclosure sale, the court, instead of requiring them to pay the amount of their bid in cash, and then applying the cash in payment of their bonds, may allow them to turn in their bonds in payment at a valuation equal to what they will be entitled to receive on distribution.<sup>224</sup> Or they may be permitted to do so by a provision to such effect in the mortgage or deed of trust.225
- (g) Estoppel and laches.—A stockholder, or bondholder, or a general creditor, who consents to a foreclosure sale, or who takes part in a reorganization of the corporation after such a sale, is estopped, in the absence of fraud, to attack the

220 Central Trust Co. v. Carter (C. C. A.) 78 Fed. 225.

221 Lehigh Coal & Navigation Co. v. Central R. Co., 34 N. J. Eq. 88, where it was held that they could provide that the bonds should be payable on or before maturity.

<sup>222</sup> White v. Wood, 129 N. Y. 527, 142 N. Y. 656.

Y.) 331, 156 N. Y. 491.

<sup>224</sup> Easton v. German American Fed. 100.
 Bank, 127 U. S. 532.

Ohio R. Co., 3 Woods, 597, Fed. Cas. No. 4,139; Farmers' Loan & Trust Co. v. Green Bay & Minnesota R. Co., 6 Fed. 100; Moran v. Hagerman (C. C. A.) 64 Fed. 499.

As to the terms of such an order, see American Water Works Co. of Illinois v. Farmers' Loan & 12 N. Y. 656. Trust Co. (C. C. A.) 73 Fed. 956; 223 Cox v. Stokes, 78 Hun (N. Farmers' Loan & Trust Co. v. Green Bay & Minnesota R. Co., 6

ank, 127 U. S. 532.

225 Child v. New York & New See, also, Duncan v. Mobile & England R. Co., 129 Mass. 170.

sale or reorganization as invalid, and sue to set it aside.226 And his right to relief, even when he has not participated in the reorganization, may be barred by laches. He must act promptly in asserting his rights, and in applying to the court for relief if they are denied.227

(h) Right to participate in reorganization.—Any party to a reorganization agreement, whether a bondholder, stockholder, or general creditor, or any person who is thereby offered the privilege of coming in, has a right to be admitted, and to participate in the benefits of the organization, provided he applies to come in within the time fixed by the agreement or offer, and complies or offers to comply with the prescribed terms or conditions. If the right is denied him, he may specifically enforce the same in the courts,228 or he may maintain an action to recover the damages sustained by reason of the refusal.229

On the other hand, neither stockholders, bondholders, nor general creditors of the corporation can claim any rights in the new organization except such as may be given them by the reorganization agreement. Those who are not parties to this agreement can claim no interest in the new company, nor sue

226 Crawshay v. Soutter, 6 Wall. (U. S.) 739; Symmes v. Union Trust Co. of New York, 60 Fed.

Where a plan for reorganization of a railroad company is not prohibited by law, one who purchases stock, after the plan is adopted, from a stockholder who voted for such plan, cannot insist that it is ultra vires. Hollins v. St. Paul, Minneapolis & M. R. Co., 29 N. Y. St. Rep. 208, 9 N. Y. Supp. 909.

A reorganization of a corporation after a foreclosure sale of its property cannot be defeated by one who purchased stock after the plan of reorganization had been adopted and partially carried out, nor by stockholders who approved and subscribed to such plan in re- Reading Trust Co. v. Reading Iron spect of part of their stock. Works, 137 Pa. St. 282.

Symmes v. Union Trust Co. of New York, 60 Fed. 830.

227 Ashhurst's Appeal, 60 Pa. St. 290; Wetmore v. St. Paul & Pacific R. Co., 3 Fed. 177; Twin Lick Oil Co. v. Marbury, 91 U. S. 587; Foster v. Mansfield, Coldwater & L. M. R. Co., 146 U. S. 88; Carey v. Houston & Texas Central Ry. Co., 52 Fed. 671. Purescent St. 52 Fed. 671; Burgess v. St. Louis County R. Co., 99 Mo. 496; Kitchen v. St. Louis, Kansas City & N. Ry. Co., 69 Mo. 224.

228 Cornell v. Utica, Ithaca & E. R. Co., 61 How. Pr. (N. Y.) 184; Marie v. Garrison, 83 N. Y. 14; Wetmore v. St. Paul & Pacific R. Co., 5 Dill. 531, 3 Fed. 177; Kelly v. Browning, 113 Ala. 420.

229 Harris v. Davis, 44 Fed. 172;

to set the sale and reorganization aside, unless they have been fraudulently or wrongfully excluded.230

It is usual and lawful to insert in an agreement for reorganization a provision that stockholders, bondholders, or other creditors who are permitted to come into the reorganization shall do so, if at all, within a certain time, and, if they refuse or fail to do so, they can claim no right to participate.231 And the same is true of other valid terms of the agreement. such as a provision that bondholders shall deposit their bonds with the reorganization committee, 232 or that stockholders or bondholders shall pay assessments or a certain sum towards the expenses of the reorganization.233

Even when the reorganization agreement fixes no time within which bondholders or stockholders must come in, they may lose their right to come in by waiting until after reorganiza-

231 Bound v. South Carolina R. Co. (C. C. A.) 78 Fed. 49, affirming 71 Fed. 53; Thornton v. Wabash Ry. Co., 81 N. Y. 462; Vatable v. New York, Lake Erie & W. R. Co., 96 N. Y. 49; Landis v. Western Pennsylvania R. Co., 133 Pa. St. 579. See infra, this section, (h)(3). 232 Carpenter v. Catlin, 44 Barb.

(N. Y.) 75.

233 Dow v. Iowa Central Ry. Co., 144 N. Y. 426; Vatable v. New York, Lake Erie & W. R. Co., 96 N. Y. 49. See infra, this section, (h)(3).

parties who held mortgage bonds

230 Shaw v. Little Rock & Ft. take in lieu thereof bonds to be Smith R. Co., 100 U. S. 605; Gates issued in a reorganization of the v. Boston & New York Air Line R. company. There was no stipula-Co., 53 Conn. 333; Terbell v. Lee, tion in the agreement as to which 40 Fed. 40; Pennsylvania Trans-of the bondholders should purchase roorted to Co., Appeal 101 Be St. portation Co.'s Appeal, 101 Pa. St. the property, nor as to contribution towards the expenses of the sale and of the reorganization. A., one of the bondholders, undertook to buy at the sale, but the property was bid above his limit, and sold to another party, who subsequently transferred the title to A. for advances made to him and other indebtedness. A. began to reorganize the company, and requested the other parties to the agreement to join in the payment of expenses, which they refused to do; and they afterwards filed a bill in equity against A. for an account of the proceeds in his hands. 1)(3). It was held that, conceding that In a Pennsylvania case, several the purchase and reorganization were in pursuance of the agreeof a railroad company, about to be ment, and were therefore to inure sold out on foreclosure of the to the benefit of all the parties mortgage, entered into an agree-thereto, yet the latter were dement that, in case of the purchase barred, by their refusal to share of the railroad in their interin the expenses, from claiming est as bondholders, they would any share in the purchase. Apnot claim their proportion of the peal of Fidelity Insurance, Trust & proceeds of the sale, but would Safe Deposit Co., 106 Pa. St. 144. tion.234 And when they are allowed to come in after the reorganization, they may lose the right to do so by unreasonable delay.235

If the agreement allows stockholders to come in if they apply within a certain time, the fact that a stockholder who applies after the time specified was ignorant of the agreement until after the expiration of the time gives him no right to come in, but his only remedy, if he has any remedy at all, is by suit to set aside the foreclosure.236

When a statute provides that any stockholder may come in and assent to a plan of reorganization of a railroad company at any time within six months after a foreclosure sale, and thereby become entitled to share in the benefits thereof, upon compliance with its terms, assent within the time specified is a condition precedent to a stockholder's right to come in. and, if he fails to assent within such time, a court of equity can give him no relief.237

(i) Illegality in reorganization agreements.—A reorganization agreement must not be illegal. If it contemplates violation of any law of the state, it is an illegal agreement, and cannot be enforced. Such is the case, for example, where a reorganization agreement provides for an issue of stock or bonds in violation of a constitutional or statutory prohibition against a fictitious increase of the stock or indebtedness of a corporation, or the acceptance of labor or property in payment of stock or bonds at a greater value than the market price at the time the labor is done or the property delivered.<sup>238</sup> This prohibition is elsewhere considered.239

A contract between the majority stockholders of a corpora-

<sup>71</sup> Fed. 53; Skiddy v. Atlantic, Pa. St. 579. Mississippi & O. R. Co., 3 Hughes, 287 Vatable 320, Fed. Cas. No. 12,922; Carpenter v. Catlin, 44 Barb. (N. Y.) 75. 285 See Holland v. Cheshire R.

Co., 151 Mass. 231; Alsop v. Riker, A.) 85 Fed. 345. 155 U.S. 448.

<sup>236</sup> Thornton v. Wabash Ry. Co.,

<sup>234</sup> Bound v. South Carolina R. 81 N. Y. 462. See, also, Landis v. Co. (C. C. A.) 78 Fed. 49, affirming Western Pennsylvania R. Co., 133

<sup>&</sup>lt;sup>237</sup> Vatable v. New York, Lake Erie & W. R. Co., 96 N. Y. 49, reversing 11 Abb. N. C. 133.

<sup>238</sup> Altenberg v. Grant (C. C. 239 Post, § 391.

The carrying out of an agree-

tion of a particular state and other persons for the reorganization of the company on a plan which would render it illegal under the laws of that state, as creating a fictitious increase of stock, cannot be presumed to contemplate a reorganization under the laws of some other state, wherein such a reorganization might be valid, where it appears that the owners of the majority of stock in the old corporation are residents of the former state, that the business of the new corporation is to be carried on in that state, and is to be of a quasi public character, and that the contract was made in that state.240

A reorganization is illegal and void if it contemplates the commission of a fraud upon stockholders, bondholders, or other creditors of the corporation, and no action will lie upon it. This is true, for example, of an agreement under which the stockholders of a corporation, whose property is about to be sold under a mortgage, are to share in the proceeds of the sale, the agreement being made for the purpose of preventing them from resisting a foreclosure, for such an agreement is a fraud upon the general creditors of the corporation.<sup>241</sup>

(j) Intention to create monopoly.—When a proposed reorganization is attacked as illegal on the ground that the business. of the new corporation will be in violation of law, the fact must affirmatively appear, the presumption being that there is no intention to engage in an illegal business, or otherwise violate the law. It has been held, therefore, that where the property of a corporation is about to be sold in judicial pro-

new corporation to be organized 287. by the bondholders, and by which the new corporation is to issue to them new mortgage bonds and full paid up stock in lieu of the old bonds, without any payment of R. Co. v. Howard, 7 Wall. (U. S.) money, does not violate a consti-392. See supra, this section, (c)tutional provision that no private (9).

ment between the holders of mort- corporation shall issue stock or gage bonds of an embarrassed rail- bonds except for money or proproad company, by which the property actually received, or labor erty and franchises of the company done, and that all fictitious inare to be purchased by trustees at crease of stock or indebtedness a sale on foreclosure of the mort-shall be void. Memphis & Little gage, and conveyed by them to a Rock Railroad v. Dow, 120 U. S.

> 240 Altenberg v. Grant (C. C. A.) 85 Fed. 345.

ceedings, the court cannot entertain objections to the purchase thereof by a committee of the bondholders or stockholders, based upon the ground that the corporation has attempted to create a trust or monopoly, and that the proposed purchasers will also endeavor to do so. The court cannot assume that any improper use will be made of the property, or undertake to control it after it has been sold and conveyed by the receiver.<sup>242</sup>

(k) Rights and remedies against new corporation. We have already considered the question as to the liability of the newcorporation, after reorganization, for the debts and contracts of the old corporation.<sup>243</sup> It is proposed to speak here of those liabilities only which are imposed by or arise out of the reorganization agreement.244

As we have seen in a former chapter, a corporation is not bound by the contracts made by its promoters unless it expressly or impliedly adopts or ratifies the same after its organization. But it is liable if it adopts or ratifies the same, and it does so if it accepts the benefit of them, as by taking a conveyance of property thereunder.<sup>245</sup> These principles apply to contracts made by the promoters of a reorganization.<sup>246</sup>

Where the holders of mortgage bonds of a corporation take, in satisfaction of their bonds, a conveyance of the mortgaged property to trustees for their benefit, form a corporation to take the property, and enter into an agreement by which the corporation, in consideration of the conveyance of the property to it, is to assume certain burdens and obligations towards them, the corporation, when it is formed, is not bound by the agreement, unless it expressly or impliedly ratifies or adopts the same; but it does impliedly adopt the agreement if it accepts a conveyance of the property, and in such a case it is bound by its terms in favor of the bondholders. In accepting the benefits of the agreement, it assumes the obligations.

In a late New York case it was said, speaking of a land

<sup>242</sup> Olmstead v. Distilling & Cat- the old company assumed by it, tle Feeding Co., 73 Fed. 44.

248 Ante, § 342.

244 As to its liability for debts of see ante, § 342(g). 245 Ante, § 101.

<sup>246</sup> Providence Albertype Co. v.

company organized to take land which had been conveyed to trustees for the benefit of the holders of bonds secured by a mortgage thereon: "The bondholders were the promoters of the land company. Being about to form a corporation for an authorized purpose, they made an agreement upon the subject in which they provided for benefits to be conferred upon it and burdens to be assumed by it after its organization. While it could have refused, when it came into existence, to accept the one or to be bound by the other, it could not accept the advantages and then refuse to assume the obligations. accepting title to the land it adopted and ratified the agreement entered into by all its stockholders, and thereby voluntarily made itself a party thereto and became bound thereby. The adoption by the land company of the contract between the bondholders was a reasonable means of carrying into effect its authorized objects, and, after knowingly receiving the benefit of the arrangement, 'it cannot be permitted to deny that it agreed to assume the corresponding burdens." "247

---Obligation to issue stock to persons entitled.--When a corporation is organized for the purpose of taking the property and franchises and carrying on the business of existing corporations, under an agreement between all the stockholders of the old corporations, under which the new corporation is to pay for the property and franchises by apportioning to them all of its stock except such as is reserved for the use of the treasury, and the transfer is made by the old corporations to the new in pursuance of the arrangement, the new corporation assumes a contract duty to each of the stockholders of the old to deliver to him his proportion of its stock, and they may maintain their actions against it if it refuses to perform the same. They are not required to seek relief through the original corporations.248

Where a corporation is organized to take over the business

Kent & Stanley Co., 19 R. I. 561; 247 Rogers v. New York & Rogers v. New York & Texas Land Co., 134 N. Y. 197, 211. Co., 134 N. Y. 197.

<sup>247</sup> Rogers v. New York & Texas <sup>248</sup> Anthony v. American Glucose Co., 146 N. Y. 407.

and assets of another, and enters into a contract with the latter and its stockholders, in consideration of a transfer of such business and assets, to issue to each of the old stockholders certificates of its stock, share for share, upon surrender of their certificates of stock in the old company, a holder of a certificate of stock in the old company may maintain a suit against the new company for specific performance of the contract, and he may do so without making the old company or any other stockholders parties defendant, or declaring that the suit is brought for the benefit of such of the old stockholders as may come in and be made parties.249

-Right to dividends-Laches.-Where the stock of an expiring corporation is merged into the stock of a new one, organized as its successor, acquiring its franchises and assuming its obligations, a provision inserted in the charter of the new company, forfeiting dividends not claimed within three years from the time when they are declared, is not binding upon the old stockholders, except from the time when, expressly or by implication, they consent thereto by assuming the quality of stockholders in the new company. An old stockholder who has been ignorant of his rights and of the transfer, and who claims his dividends as soon as informed of their existence, cannot be affected by such provision except in the future.250

ized, new stock issued, and the old of the old stockholders in proporstock canceled, and a purchaser of tion to his shares, on payment of the stock in the reorganized com- the par value thereof in cash, and pany demands its issue to him the business of the old company is within a month after his purchase, closed, and its stock declared canand the demand is refused, and celed, a subsequent purchaser of such stockholder fails for seven shares of stock in the old company years to assert his rights under the cannot compel the reorganized compurchase, his laches are a bar to pany to issue stock to him in lieu any relief. Stoddard v. Decatur of the interest so purchased. Stod-Cracker Co., 148 Ill. 53, affirming 84 Ill. App. 374.

Where the stockholders of an embarrassed corporation vote to reorganize the same, apply its assets in payment of its debts, cancel the old stock, and issue stock in rollton R. Co., 41 La. Ann. 1020.

When a corporation is reorgan- the reorganized corporation to each dard v. Decatur Cracker Co., 184 Ill. 53, affirming 84 Ill. App. 374.

> 249 Fletcher v. Newark Telephone Co., 55 N. J. Eq. 47.

250 Amant v. New Orleans & Car-

§ 3451

-Stockholder's right in surplus transferred from old corporation.—Where a corporation is dissolved, and a new corporation formed, and all the assets of the old corporation, including a surplus, are transferred to the new corporation, a stockholder of the old corporation who receives for his interest an equal number of shares in the new corporation, and who allows the matter to rest after his demand for a share of the surplus is refused, waives any right in such surplus except as a stockholder in the new corporation, and cannot afterwards assert a right thereto when the corporation has become insolvent.<sup>251</sup>

-- Corporation as bona fide purchaser.-- When the property of a corporation is conveyed by it to trustees for the benefit of its mortgage bondholders, and in satisfaction of the bonds, and the bondholders enter into an agreement under which a corporation is to be formed for the purpose of taking and holding the property, and under which the corporation is to assume certain burdens and obligations towards them, the corporation, when formed in pursuance of the agreement and when it takes a conveyance of the land, paying nothing therefor, is not in the position of a bona fide purchaser as against the bondholders asserting rights under the agreement, although it may have assumed certain duties with reference to the property.<sup>252</sup>

(1) Liability to tax.—Under a statute providing that every corporation organized under the general or special laws of the state shall pay a certain tax, a corporation formed upon a reorganization is liable to the tax, if it is a new corporation, but not otherwise. A corporation formed under a reorganization following a foreclosure sale is a new corporation, and liable to the tax.253

Land Co., 134 N. Y. 197, 211.

<sup>253</sup> People v. Cook, 110 N. Y. 443, affirming 10 N. Y. St. Rep.

§ 339.

 251 Boynton v. Roe, 114 Mich. under the New York manufacturing act of 1848 was reorganized
 252 Rogers v. New York & Texas under the provision of Laws 1890, c. 567, § 5, declaring that "any corporation heretofore organized," etc., on the vote of a majority of stock, and the filing of a certifi-As to what constitutes the creacate, which, among other things, tion of a new corporation, see ante, must contain the statements required in the certificate of a corpo-Where a corporation organized ration originally formed under the

(m) Statutory provisions for reorganization—(1) Power of legislature.—In most of the states, if not in all, there are statutory provisions for the reorganization of corporations, and these provisions are binding, of course, except in so far as they may be in violation of constitutional prohibitions. In the United States, the legislatures may undoubtedly prescribe any terms and conditions they may see fit in authorizing reorganizations. provided they violate no constitutional prohibition; but the constitutional prohibition against laws impairing the obligation of contracts prevents them from depriving any stockholder. bondholder, or creditor of a corporation of the rights secured to him by his contract. In the United States, therefore, a legislature cannot deprive a mortgage bondholder of a corporation of the right to the benefit of his security by authorizing a majority of the bondholders to force him into a reorganization without a foreclosure of the mortgage. 254 may, however, prevent him from coming into a reorganization of the corporation without complying with certain terms, unless the right to do so is given him by his contract, provided he is not deprived of his right to share in the proceeds of the mortgaged property.255

In England and Canada, where there is no such constitutional limitation on the power of the legislature, the same rule does not apply, but parliament may authorize a corporation or a majority of the stockholders or bondholders in a corporation to force a settlement and reorganization upon the minority. <sup>256</sup> And it has been held by the supreme court of the United States that the proceedings under such a statute will be binding upon

act of 1890, and further declaring that, from the time of filing the new certificate, "such corporation" should be "deemed to be a corporation organized under" such chapter, it was held that the reorganized corporation was a new corporation, and, as such, subject to the franchise tax imposed by Laws 1886, c. 143. In re New York & Suburban Investment Co., 16 N. Y. Supp. 213.

<sup>254</sup> See Canada Southern Ry. Co. v. Gebhard, 109 U. S. 527.

<sup>255</sup> See Gilfillin v. Union Canal Co., 109 U. S. 401; Vatable v. New York, Lake Erie & W. R. Co., 96 N. Y. 49.

<sup>256</sup> Nicholl v. Eberhardt Co., 61 Law T. (N. S.) 489; In re London Chartered Bank of Australia [1893] 3 Ch. Div. 540; Canada Southern Ry. Co. v. Gebhard, 109 U. S. 527. bondholders who are citizens of the United States. In the case referred to, the Canadian parliament had authorized a Canadian railroad company to enforce a settlement upon the holders of mortgage bonds of the company, by which they should receive other securities in the company in the place of their bonds, and the statute provided for participation in the reorganization of the company on equal terms by citizens of the United States holding bonds of the company. The settlement went into effect with the assent of a majority of the bondholders, and it was held binding upon nonassenting bondholders who were citizens of the United States, so that they could not afterwards maintain a suit to recover on the bonds in the courts of the United States.

It was said in substance by Chief Justice Waite: ers of bonds and other obligations issued by large corporations for sale in market, and secured by mortgages to trustees, or otherwise, have, by fair implication, certain contract relations with each other. They are not corporators, and thus necessarily, in the absence of fraud or undue influence, bound by the will of the majority as to matters within the scope of the corporate powers, but they are interested in the administration of a trust which has been created for their common benefit. Ordinarily their ultimate security depends in a large degree on the success of the work in which the corporation is engaged, and it is not uncommon for differences of opinion to exist as to what ought to be done for the promotion of their mutual interests. In the absence of statutory authority or some provision in the instrument which establishes the trust, nothing can be done by a majority, however large, which will bind a minority without their consent. Hence it seems to be eminently proper that where the legislative power exists some statutory provision should be made for binding the minority in a reasonable way by the will of the majority; and unless, as is the case in the states of the United States, the passage of laws impairing the obligation of contracts is forbidden, we see no good reason why such provision may not be made in respect to existing as well as prospective obligations. The nature of securities of this class is such that the right of legislative supervision for the good of all, unless restrained by some constitutional prohibition, seems almost necessarily to form one of their ingredients; and when insolvency is threatened, and the interests of the public, as well as creditors, are imperiled by the financial embarrassments of the corporation, a reasonable scheme of arrangement may, in our opinion, as well be legalized as an ordinary composition in bankruptcy. In fact, such arrangement acts are a species of bankrupt acts. Their object is to enable corporations created for the good of the public to relieve themselves from financial embarrassments by appropriating their property to the settlement and adjustment of their affairs, so that they may accomplish the purposes for which they were incorporated. In no just sense do such governmental regulations deprive a person of his property without due process of law. They simply require each individual to so conduct himself for the general good as not unnecessarily to injure another."257

- —(2) Implied assent of parties.—If the legislature, in authorizing the reorganization of corporations, allows stockholders or bondholders to come in within a certain time, and consent to or vote upon a plan of reorganization, and provides that those who do not vote shall be deemed to have assented, the provision is valid, and will be given effect.<sup>258</sup>
- —(3) Compliance with terms and conditions of statute.—When the persons interested in a corporation undertake to reorganize under a statute providing for reorganization, they must comply with its terms. A person who does not comply with its terms, although he may not lose his rights as against the old corporation and its property, acquires no right to share in the reorganization. For example, if a statute provides that any stockholder may come in and assent to a plan of reorgan-

<sup>257</sup> Canada Southern Ry. Co. v. 258 Union Canal Co. v. Gilfillin, Gebhard, 109 U. S. 527. 93 Pa. St. 95; Gilfillin v. Union Canal Co., 109 U. S. 401.

ization of a railroad company at any time within six months after a foreclosure sale, and thereby become entitled to share in the benefits thereof, upon compliance with its terms, a stockholder who does not come in and assent within the six months has no right to come in, and a court of equity cannot relieve him from the effect of his delay.259 The same is true of other terms.260

—(4) Reorganization independently of the statute.—Unless there is something to show a contrary intent upon the part of the legislature, a statute authorizing the reorganization of corporations, and préscribing a particular mode, is merely cumulative, and does not exclude the right of the purchasers of the franchises and property of a corporation to organize as a new corporation under general laws.261

Where a statute provided that the purchasers of railroads, turnpikes, etc., under foreclosure, should have the franchises and privileges of the corporation owning the road purchased, and declared that they should be a distinct corporation under such name as might be assumed by them, provided they should proceed to organize within three months under the old charter, etc., it was held that the statute was permissive merely, and that it did not prohibit such purchasers from organizing as a corporation of the like kind, after the three months, under the general laws.262

Erie & W. R. Co., 96 N. Y. 49, reversing 11 Abb. N. C. 133.

<sup>260</sup> Under Acts N. Y. 1874, c. 430, to facilitate the reorganization of railroads sold under mortgage, and providing for the formation of new companies in such cases, it was that they had no notice. Vatable held that a stockholder in the old company had a right to join the Co., 96 N. Y. 49, reversing 11 Abb. new only on compliance with N. C. 133. the terms of the plan of reorganization; that the projectors of the plan were not required to provide for a notice; and notice having been given by publication, to the See State v. Hare, 121 Ind. 308.

<sup>259</sup> Vatable v. New York, Lake effect that certain payments must be made by stockholders wishing to join the new organization, stockholders failing to make the required payments within the time limited could not afterwards claim the right to come in, on the ground v. New York, Lake Erie & W. R.

<sup>261</sup> Moore v. State, 71 Ind. 478; Jeffrey v. Moran, 101 U. S. 285.

262 Moore v. State, 71 Ind. 478.

## § 346. Promotion of reorganizations.

It needs no argument to show that the promoters of the reorganization of a corporation are in substantially the same position with respect to the new corporation and those who become members as the promoters of any other corporation.<sup>263</sup> They occupy a fiduciary relation, and will not be permitted to make a secret profit out of the reorganization, or to obtain any other advantage over the other parties who become members of the corporation.264

As in the case of original incorporation, promoters of a reorganization cannot bind the new corporation by contracts before its formation, nor after its formation, unless they are its duly-constituted agents. But contracts made by them may be adopted or ratified by the corporation when formed, as in other cases.265

The promoters of a corporation are personally liable on contracts made by them in the course of the reorganization, as for services performed by others in connection with the reorganization, unless there is an understanding to the contrary.266

## II. CONSOLIDATION OF CORPORATION S.

§ 347. In general.—The consolidation of corporations is a combination of two or more existing corporations, by an agreement between them, under legislative authority, under which the old corporations are dissolved, and a new corporation created, or one corporation is continued, and the other or others are merged in it.

Corporations have no power to consolidate, unless the power is

an injunction has been issued and a receiver appointed, take steps looking towards a reorganization and a resumption of its property and business; and it consequently may, in exercising that power, employ agents, and incur liability to compensate them, which may be 266 Ante. § 107; Babbitt v. Gibbs, enforced on the dissolution of the injunction and the removal of the A corporation may, after it has receiver. Linn v. Joseph Dixon been declared insolvent, and after Crucible Co., 59 N. J. Law, 28.

<sup>263</sup> See ante, § 99 et seq.

<sup>264</sup> See ante, § 110.

<sup>265</sup> Ante, § 101; Providence Albertype Co. v. Kent & Stanley Co., 19 R. I. 561; Rogers v. New York & Texas Land Co., 134 N. Y. 197, 211; ante, § 345(d).

<sup>150</sup> N. Y. 281.

expressly conferred by their charters, or by the charter of one of them, or by some other statute, and the consolidation must be effected in compliance with the terms of the statute. But the legislature may ratify an unauthorized or defective consolidation.

When corporations are consolidated under legislative authority, the general rules are that—

- (1) The consolidated corporation acquires all the property, rights, powers, franchises, and privileges of the consolidating corporations, subject to the same burdens and restrictions which attached thereto in the hands of the consolidating corporations, respectively, under their charters.
- (2) And it is directly liable for the debts, on the contracts, and for the torts of the consolidating corporations.
- (3) These rules may be changed, however, subject to some limitations, by the statute authorizing the consolidation, or by the articles or agreement of consolidation.

When a consolidating corporation is dissolved by the consolidation, it cannot afterwards sue or be sued, and actions pending by or against it abate, unless there is statutory provision to the contrary. But if the right or liability passes to the consolidated corporation, it may be substituted as a party.

Corporations created by or under the laws of different states may be consolidated under concurrent legislation in each state, so as to be a consolidated company for the purpose of transacting business, etc., but technically, in contemplation of the law, there is a separate and distinct corporation in each state.

## § 348. What constitutes a consolidation.

The consolidation of corporations means, generally, the combination of two or more corporations of the same or different <sup>267</sup> states, by an agreement between them, <sup>268</sup> under legislative authority, <sup>269</sup> by which their rights, franchises, privileges, and property are united, and become the rights, franchises, privileges, and property of a single corporation, composed generally, although not necessarily, of the stockholders of the original corporations. <sup>270</sup> The corporation resulting

<sup>&</sup>lt;sup>267</sup> See post, § 362, as to the consolidation of corporations of different states.

<sup>&</sup>lt;sup>268</sup> See post, § 350.

 <sup>269</sup> See post, § 349.
 270 Atlantic & Gulf R. Co. v.

from the consolidation is called the consolidated corporation, and the original corporations are called the consolidating or constituent corporations.

Creation of new corporation not necessary.—Ordinarily, the consolidating corporations are dissolved by the consolidation, and cease to exist, and an entirely new and distinct corporation is created as of the time of the consolidation.<sup>271</sup> formerly thought that this was always the effect of a consolidation, but it is now well settled that it is not necessarily so, and that a consolidation may be effected by the merger of one corporation in another, and continuance of the latter with the rights, franchises, privileges, and property of the former in addition to its own.272 "When the rights, franchises, and effects of two or more corporations are, by legal authority and agreement of the parties, combined and united into one whole, and committed to a single corporation, the stockholders of which are composed of those (so far as they choose to become such) of the companies thus agreeing, this is in law, and according to common understanding, a consolidation of such companies; whether such single corporation, called the consolidated company, be a new one then created, or one of the original companies, continuing in existence with only larger rights, capacities and property." 278

stock of another corporation is not, of itself, sufficient to show a 603, 656.

Georgia, 98 U. S. 359, 1 Keener's Cas. 129. And see post, § 354, where many other cases are cited. 16 Ind. 172, 79 Am. Dec. 418; People v. New York, Chicago & St. L. R. Co., 129 N. Y. 474, 1 Keener's Co. v. Georgia, 92 U. S. 665, 1 Keener's Cas. 129; Chicago, Santa Fe & C. Ry. Co. v. Ashling, 160 Ill. 373.

The mere fact that one corporation has obtained control of the cases and illustrations.

273 Meyer v. Johnston, 64 Ala.

consolidation. Jessup v. Illinois Central R. Co., 36 Fed. 735.

271 Atlantic & Gulf R. Co. v. Georgia, 98 U. S. 359, 1 Keener's Cas. 107; McMahan v. Morrison, 16 Ind. 172, 79 Am. Dec. 418; People v. New York, Chicago & St. L. R. Co., 129 N. Y. 474, 1 Keener's their respective articles of asso-

Purchase and consolidation distinguished.—The mere purchase by one corporation of the property and franchises of another, either directly from the latter, or at an execution or foreclosure sale, does not operate as a consolidation of the two corporations, in the absence of express statutory provision to this effect.<sup>274</sup> But it has been held that a consolidation, and not a mere purchase by one corporation of the property and franchises of another, is effected by a transfer of all the property, stock, and franchises of one corporation to another under an arrangement by which the stock of the latter is issued to the stockholders of the former in exchange for their stock.<sup>275</sup>

Corporations of different states.—As we shall see at some length in a subsequent section, corporations created by different states may be consolidated under concurrent legislation of each state, but in such a case, since the laws of a state have no operation beyond its limits, and cannot create or aid in creating a corporation in another state, there is, in law, a separate and distinct corporation in each state.<sup>276</sup>

## § 349. Power to consolidate.

(a) Necessity for legislative authority.—The consolidation of corporations is not within the objects of a corporation, in the absence of provision therefor, and cannot be implied. It is well settled, therefore, that corporations cannot lawfully consolidate, however desirable and beneficial consolidation may be, unless the state has expressly authorized them to do

ciation, and to register themselves under new articles as one body." In re Bank of Hindustan, China & Japan, 2 Hem. & M. 657, 666. But in a later case it was said that "two companies may be united either by fusion into a third, or by one absorbing the other." In re Empire Assurance Corp., 28 Law T. (N. S.) 60, 62.

<sup>274</sup> Gulf, Colorado & S. F. Ry. Co. v. Newell, 73 Tex. 334, 15 Am.

St. Rep. 788. And see the dissenting opinion of Craig, C. J., in Chicago, Santa Fe & C. Ry. Co. v. Ashling, 160 Ill. 373.

<sup>275</sup> Chicago, Santa Fe & C. Ry. Co. v. Ashling, 160 Ill. 373. See, also, Chicago & Eastern Illinois R. Co. v. State, 153 Ind. 134. Compare Rafferty v. Buffalo City Gas Co., 37 App. Div. (N. Y.) 618.

276 Post, § 362.

so, either by a provision in their charters, or the charter of one of them, or by a special act passed after their creation, and before consolidation, provided a special act for such a purpose is constitutional, or by a general law. Legislative authority is just as essential to a valid consolidation of existing corporations as it is to the creation of a corporation in the first instance.277 It follows that an agreement between two or more corporations to consolidate, in the absence of legislative authority, is ultra vires, and will not be enforced, even though it may have been partly performed.278

(b) How authority to consolidate is conferred.—Authority to consolidate may be conferred upon corporations by a provision in their charters, or in the charter of one of them; 279 or it may be conferred by a special act passed after their creation,280 subject to the rights of stockholders,281 and provided such an act is not in violation of a constitutional prohibi-

277 Pearce v. Madison & Indian- & Mississippi Valley R. Co., 77 apolis R. Co., 21 How. (U. S.) 442, 1 Keener's Cas. 454, 1 Cum. Cas. 146; Clearwater v. Meredith, 1 Wall. (U. S.) 25; Kavanagh v. Omaha Life Ass'n, 84 Fed. 295; American Loan & Trust Co. v. Minnesota & Northwestern R. Co.. 157 Ill. 641; State v. Bailey, 16 Ind. 46. 79 Am. Dec. 405; Aspinwall v. Ohio & Mississippi R. Co., 20 Ind. 492; State v. Beck, 81 Ind. 500; Crawfordsville & Darlington Turnpike Co. v. State, 102 Ind. 435; Tuttle v. Michigan Air Line R. Co., 35 Mich. 247; Greenville Compress & Warehouse Co. v. Planters' Compress & Warehouse Co., 70 Miss. 669, 35 Am. St. Rep. 681; Black v. Delaware & Raritan Canal Co., 24 N. J. Eq. 455; New York & Sharon Canal Co. v. Fulton Bank, 7 Wend. (N. Y.) 412; Cole v. Millerton Iron Co., 133 N. Y. 164, 28 Am. St. Rep. 615; Blatchford v. Ross, 54 Barb. (N. Y.) 42; Lauman v. Lebanon Valley R. Co., 30 Pa. St. 42, 72 Am. Dec. 695; Gulf, Colorado & S. F. Ry. Co. v. Newell, 73 Tex. 334, 15 Am. St. Rep. 788; Adams v. Yazoo

Miss. 194; Topeka Paper Co. v. Oklahoma Publishing Co., 7 Okla.

This is also the rule in England. East Anglian Ry. Co. v. Eastern Counties Ry. Co., 11 C. B. 775, 1 Keener's Cas. 450, 1 Cum. Cas. 142; Great Northern Ry. Co. v. Eastern Counties Ry. Co., 9 Hare, 306; Charlton v. Newcastle & Carlisle Ry. Co., 5 Jur. (N. S.) 1096; Clinch v. Financial Corporation, L. R. 5 Eq. 450.

278 Greenville Compress & Warehouse Co. v. Planters' Compress & Warehouse Co., 70 Miss. 669, 35 Am. St. Rep. 681; post, § 351. See ante, § 213 et seg.

<sup>279</sup> See Nugent v. Supervisors, 19 Wall. (U. S.) 241; Sparrow v. Evansville & Crawfordsville R. Co., 7 Ind. 369.

280 See Black v. Delaware & Raritan Canal Co., 24 N. J. Eq. 455; Fisher v. Evansville & Crawfordsville R. Co., 7 Ind. 412.

281 See infra, this section, (f).

tion.<sup>282</sup> In most of the states, authority to consolidate is conferred upon corporations, or upon corporations of a particular class, by a general law prescribing the mode and terms in and upon which the consolidation may be effected. The New York statute may be given as an illustration. The business corporations law of that state provides that "any two or more corporations organized under the laws of this state for the purpose of carrying on any kind of business of the same or of a similar nature, which a corporation organized under this chapter might carry on, may consolidate such corporations into a single corporation," in the manner therein pointed out, provision being made for an agreement between the corporations to consolidate, signed by a majority of their respective boards of directors, and under their respective corporate seals, prescribing the terms and conditions of the same, the mode of carrying it into effect, the name of the new corporation, the number of directors who shall manage its affairs, not less than three, nor more than thirteen, the names and post-office addresses of the directors for the first year, the term of its existence, not exceeding fifty years, the name of the town or towns, county or counties, in which its operations are to be carried on, the name of the town or city and county in which its principal place of business is to be situated, the amount of its capital stock, which shall not be larger in amount than the fair aggregate value of the property, franchises, and rights of such corporations, and the number of shares into which the same is to be divided, the manner of distributing such capital stock among the holders thereof, and if such corporations, or either of them, shall have been organized for the purpose of carrying on any part of its business in any place out of the state, the agreement shall so state, with such other particulars as they may deem necessary.

It is then provided that the agreement shall be submitted

<sup>282</sup> Ante, § 39(c)(4).

to the stockholders of each of such corporations, at a meeting to be called in a certain way, and that, if the agreement shall be approved at each of such meetings, by stockholders owning at least two-thirds of the stock, the same shall be the agreement of the corporations; that such agreement and a verified copy of the proceedings of such meetings shall be made in duplicate, one of which shall be filed in the office of the secretary of state, and the other in the office of the clerk of the county where the principal business office of the new corporation is to be situated in the state; and that thereupon such corporations shall be merged into the new corporation specified in such agreement, to be known by the corporate name therein mentioned, and the provisions of such agreement shall be carried into effect as therein provided.

Provision is then made for payment to dissenting stockholders of the value of their shares, to be determined by an appraisement in a manner specified in the statute.

It is then provided that the new corporation, in addition to the general powers of corporations, shall enjoy the rights, franchises, and privileges possessed by each of the corporations so consolidated, subject to the restrictions, liabilities, duties, and provisions contained in the charter, so far as the same may be applicable to the purposes for which it shall have been organized and expressed in the agreement for consolidation, and may prosecute and carry on any kind of business which each of the consolidating corporations was authorized by law to conduct.

It is then provided that, upon such consolidation and organization of such new corporation, all the rights, privileges, franchises, and interests of every kind belonging to or enjoyed by the corporations so consolidated, and every species of property, real, personal, and mixed, and choses in action, belonging to them, mentioned in the agreement for consolidation, shall be deemed to be transferred and vested in, and may be enjoyed by, such new corporation, without any other deed or

transfer; and such new corporation shall hold and enjoy the same, and all rights of property, privileges, franchises, and interests, in the same manner and to the same extent as if the several corporations so consolidated had continued to retain the title and transact the business of such corporations, and the title to real and personal property and rights and privileges acquired and enjoyed by either of the corporations shall not revert or be impaired by such consolidation, or anything relating thereto.

It is then declared that the rights of creditors of any corporation that shall so be consolidated shall not in any manner be impaired, nor any liability or obligation for the payment of any money due or to become due to any person or persons, or any claim or demand for any cause existing against any such corporation, or against any stockholder thereof, be released or impaired by any such consolidation; but such new corporation shall succeed to and be held liable to pay and discharge all such debts and liabilities of each of the corporations consolidated, in the same manner as if such new corporation had itself incurred the obligation or liability to pay such debt or damages, and the stockholders of the respective corporations consolidated shall continue, subject to all the liabilities, claims, and demands existing against them as such at or before the consolidation; and no action or proceeding then pending before any court or tribunal in which any corporation that may be so consolidated is a party, or in which any such stockholder is a party, shall abate or be discontinued by reason of such consolidation, but may be prosecuted to final judgment as though no consolidation had been entered into; or such new corporation may be substituted as a party in place of any corporation so consolidated, by order of the court in which such action or proceeding may be pending.

In other statutes of New York, special provision is made for the consolidation of gas and electric light companies, railroad companies, telegraph and telephone companies, and turnpike, plank-road, and bridge companies.

- (c) Ratification.—As we have seen in treating of the creation of corporations, a corporation may acquire a de jure existence by reason of legislative ratification or recognition of an unauthorized claim of corporate existence.283 In like manner, an unauthorized consolidation of corporations may be rendered valid by legislative ratification or recognition.<sup>284</sup>
- (d) Construction of statutes.—Whether or not a particular statute authorizes a consolidation depends, of course, upon its terms and the intention of the legislature. A statute which provides that, in case of the consolidation of corporations, the consolidated corporation shall be liable for the debts of the original companies, does not itself authorize consolidations, but applies to consolidations otherwise authorized.285

When a statute authorizes the consolidation of particular corporations only, or of corporations of a particular class only, it does not apply to other corporations, or corporations of a different class. A statute authorizing corporations theretofore organized to consolidate does not authorize the consolidation of corporations afterwards organized. 286 Some of the decisions are given in the note below.287

When a statute or charter gives a corporation power to consolidate with another corporation of a like character, without

<sup>283</sup> Ante, §§ 43(b), 77.

<sup>284</sup> Bishop v. Brainerd, 28 Conn. 289; Mead v. New York, Housa-tonic & N. R. Co., 45 Conn. 199; McAuley v. Columbus, Chicago & I. C. Ry. Co., 83 Ill. 348; Mitchell v. Deeds, 49 Ill. 416, 95 Am. Dec.

Omaha Life 285 Kavanagh v. Ass'n. 84 Fed. 295.

<sup>286</sup> Shelbyville & Rushville Turnpike Co. v. Barnes, 42 Ind. 498.

manufacturing companies, within a

Electric Illuminating Co., 96 Ala. 295, 38 Am. St. Rep. 94. See ante, § 36(e), as to what are manufacturing corporations.

The consolidation of corporations engaged in the same general line of business is not necessarily against public policy, or prohibited by a statute providing that no stock corporation shall "combine" with any other corporation for the prevention of competition. Cameron v. New York & Mount Vernon Wa-287 Electric light companies are ter Co., 62 Hun, 269, 133 N. Y. 336.

Consolidation of rival or competstatute allowing such corporations ing companies is sometimes exto consolidate. Beggs v. Edison pressly prohibited. See Watson v.

specifying any particular corporation, it authorizes a consolidation with any other corporation of the same character, whether the charter of the other corporation expressly gives it any power to consolidate or not.288

A statute in terms authorizing the consolidation of "two" corporations into a new corporation does not mean that no greater number of corporations than two can consolidate, but authorizes. by intendment, the consolidation of two or more corporations.<sup>289</sup>

(e) Withdrawal or impairment of power.—It has been held that a grant in the charter of a corporation of the power to form a union or consolidation with any other corporation is a contract between the state and the corporation, within the constitutional prohibition against laws impairing the obligation of con-

Harlem & New York Navigation Co., 145 U. S. 409; State v. Vander-Co., 52 How. Pr. (N. Y.) 348. bilt, 37 Ohio St. 590.

A statute of Louisiana authorizing the consolidation of business manufacturing corporations whose objects and business are of the same nature was held not to authorize the consolidation of two corporations, the life of one of which was to terminate at the commencement of the life of the other. New Orleans Gaslight Co.v. Louisiana Light & Heat Producing & Mfg. Co., 11 Fed. 277.

An act authorizing "railroad" companies to consolidate applies to street railroads (In re Washington Street, Asylum & Park R. Co., 115 N. Y. 442, affirming 52 Hun, 311), unless there is something to show an intention to exclude them (City of Philadelphia v. Thirteenth & Fifteenth Streets Co., 1 Leg. Gaz. Rep. [Pa.] 163).

Statutes authorizing consolidation of railroad companies may be in terms limited to connecting lines. See State v. Atchison & Nebraska R. Co., 24 Neb. 143, 8 Am. St. Rep. 164; Central Railroad & Banking Co. v. City of Macon, 43 Ga. 605, 646; Wallace v. Long Island R. Co., 12 Hun (N. Y.) 460; Livingston County v. First Nat. Bank of Portsmouth, 128 U.S. 102; Han-

According to the weight of authority, an act authorizing the consolidation of railroad companies owning connecting lines, or whose roads are so located as to permit passage of cars continuously over each other's lines, does not authorconsolidation of companies whose roads are connected by leased lines only. State v. Vanderbilt, 37 Ohio St. 590; East Line & Red River Ry. Co. v. State, 75 Tex. 434. Compare Black v. Delaware & Raritan Canal Co., 22 N. J. Eq. 130.

Such a statute does not apply to corporations owning and operating competing or parallel roads. State v. Vanderbilt, 37 Ohio St. 590; State v. Atchison & Nebraska R. Co., 24 Neb. 158, 8 Am. St. Rep. 164. See Louisville & Nashville R. Co. v. Kentucky, 161 U. S. 677.

288 In re Prospect Park & Coney Island R. Co., 67 N. Y. 371; Mitchell v. Deeds, 49 Ill. 416, 95 Am. Dec. 621; Hill v. Nisbet, 100 Ind. 341. See, also, New York & New England R. Co. v. New York, New Haven & H. R. Co., 52 Conn. 274. Compare State v. Consolidation Coal Co., 46 Md. 11.

289 People v. Rice, 66 Hun (N. cock v. Louisville & Nashville R. Y.) 130, affirmed 138 N. Y. 614, tracts,290 and that it cannot be withdrawn or impaired by subsequent legislation without the consent of the corporation.<sup>291</sup>

A grant of power to consolidate to a corporation after its creation cannot constitute a contract between the state and the corporation until it is accepted, and if it is not accepted until after the adoption of a constitutional or statutory provision reserving to the state the right to withdraw franchises or to alter or repeal charters and laws, the grant is subject to the reserved power.292

When a statute authorizing the consolidation of corporations is repealed by the legislature (assuming that the repeal is within its power as to existing corporations), proceedings to consolidate cannot afterwards be commenced. But the repeal cannot affect consolidations perfected prior thereto. Nor can it prevent completion of a consolidation commenced prior thereto, where there is a provision saving acts done or rights which have accrued. Where two corporations, having authority to consolidate under a statute, enter into an agreement to consolidate, as provided by the statute, call a stockholders' meeting to ratify the agreement, and serve and begin the publication of the required notices, before the statute is repealed, they may complete the consolidation afterwards, where the repealing act provides that it shall not affect or impair any act done or right accruing, accrued, or acquired prior thereto.293

As was shown in a former chapter, the legislature may withdraw the general power to consolidate, conferred upon a railroad corporation by its charter or a general law, to such an extent as to prohibit consolidation with parallel or competing lines, if the right to alter, amend, or repeal the charter has been reserved.294 And even in the absence of such a reservation, such

<sup>668, § 1.</sup> 

<sup>290</sup> Ante, § 268 et seq.

<sup>291</sup> Zimmer v. State, 30 Ark. 677. But see Adams v. Yazoo & Mississippi Valley R. Co., 77 Miss. 194.

<sup>292</sup> Pearsall v. Great Northern Co. v. State, 54 Ga. 401.

construing Laws N. Y. 1892, c. Ry. Co., 161 U. S. 646, 1 Keener's Cas. 264; ante, § 275(b)(10).

<sup>293</sup> Louisville & Nashville R. Co. v. Kentucky, 161 U. S. 677, 1 Keener's Cas. 282; ante, § 272(c)

<sup>294</sup> Central Railroad & Banking

a limitation of the power to consolidate is within the police power of the state.295

(f) Dissent of stockholders.—The power of a majority of the stockholders of a corporation, including the power to consolidate with another corporation, will be treated at length in a subsequent chapter,296 and it is only necessary to state the general rules in this place.

As we shall see, if the charter of a corporation, or a general law in force at the time of its formation, expressly allows the corporation to consolidate, the provision enters into and forms a part of the contracts between the corporation and the stockholders, and such a consolidation as is contemplated by the statute may afterwards be effected by a majority of the stockholders against the dissent of the minority.<sup>297</sup> In the absence of such a provision, however, the majority cannot consolidate against the dissent of the minority, even under legislative authority, for to allow the statute to have this effect would impair the obligation of the contracts between the corporation and the dissenting stockholders.<sup>298</sup> This is true, even when the legislature has reserved the power to alter, amend, or repeal the charter of the corporation, if the consolidation works a radical change in the character or objects of the corporation.<sup>299</sup> Under the power of eminent domain, the legislature may, when the public good so requires, authorize consolidation of a corporation against the dissent of stockholders, provided it makes provision for just compensation to them for their shares, whenever

Y. 336, affirming 62 Hun, 269.

296 Post, chapter xxiv.

<sup>297</sup> Sparrow v. Evansville & Crawfordsville R. Co., 7 Ind. 369; Bish v. Johnson, 21 Ind. 299; Sprague v. Illinois River R. Co., 19 Ill. 174; post, chapter xxiv.

dianapolis & Cincinnati R. Co., 4 Cas. 897.

<sup>295</sup> Cameron v. New York & Biss. 78, Fed. Cas. No. 9,891; Botts Mount Vernon Water Co., 133 N. v. Simpsonville & Buck Creek Turnpike Road Co., 88 Ky. 54; Lauman v. Lebanon Valley R. Co., 30 Pa. St. 42, 72 Am. Dec. 685; State v. Bailey, 16 Ind. 46, 79 Am. Dec. 405; Kenosha ,Rockford & R. I. R. Co. v. Marsh, 17 Wis. 13, 1 Cum. Cas. 897; post, chapter xxiv.

<sup>298</sup> Clearwater v. Meredith, 1 <sup>299</sup> Kenosha, Rockford & R. I. R. Wall. (U. S.) 25; Mowrey v. In- Co. v. Marsh, 17 Wis. 13, 1 Cum.

the corporation is of such a character that the legislature may delegate the power of eminent domain.300

If a stockholder in a corporation acquiesces in its consolidation with another corporation, and surrenders his stock for shares in the new company, he cannot complain of the consolidation, or of the terms and conditions upon which it was authorized and effected.301

-Remedies of dissenting stockholders.-If a majority of the stockholders of a corporation undertake or threaten to consolidate against the dissent of the minority, a dissenting stockholder may maintain a suit to enjoin them,302 unless such remedy is barred by laches and intervention of rights of third persons.303 If the consolidation has been effected, he may maintain an action against the consolidated corporation to recover the value of his interest in the consolidating corporation.<sup>304</sup> He may recover such value in money, and cannot be compelled to take shares of stock in the consolidated corporation.305

If a corporation is consolidated with another under legislative authority, when the legislature has not reserved the right to alter, amend, or repeal the charter, dissenting shareholders are released from liability on their subscriptions, and may set up the consolidation as a defense in an action thereon. this is true, even when the legislature has reserved the right to alter, amend, or repeal the charter, if the consolidated corporation is radically different.306 The right to set up such de-

Soo Black v. Delaware & Raritan Canal Co., 24 N. J. Eq. 455.

Sol Union Canal Co. v. Young, 1
Whart. (Pa.) 410, 30 Am. Dec. 212.

Sol Mowrey v. Indianapolis & Cincinnati R. Co., 4 Biss. 78, Fed. Cas. No. 9,891; Botts v. Simpsonville & Black Creek Turnpike Road Co., 88 Ky. 54; Lauman v. Lebanon Valley R. Co., 30 Pa. St. 42, 72 Am. Dec. 685; post, § 539.

303 Chapman v. Mad River & Lake Erie R. Co., 6 Ohio St. 119;

post, § 553.

304 Lauman v. Lebanon Valley R. Co., 30 Pa. St. 42, 72 Am. Dec. 685; Taylor v. Earle, 8 Hun (N. Y.) 1; International & Great Northern R. Co. v. Bremond, 53 Tex. 96; Ervin v. Oregon Railway & Navigation Co., 27 Fed. 635.

305 McVicker v. Ross, 55 Barb. (N. Y.) 247; Taylor v. Earle, 8 Hun (N. Y.) 1; Frothingham v. Barney, 6 Hun (N. Y.) 366.

306 Sparrow v. Evansville & Crawfordsville R. Co., 7 Ind. 369; Kenosha, Rockford & R. I. R. Co.

fense, however, may be lost by unreasonable delay in giving notice of dissent.307 There is no release, if the power to alter, amend, or repeal has been reserved, and the consolidation does not work a radical change in the character or objects of the corporation.<sup>308</sup> Nor is there any release when the charter of a corporation, or a general law in force at the time of the subscription, authorizes the consolidation. 309

(g) Dissent of creditors.—The consent of the creditors of a corporation is not necessary to its consolidation. They cannot prevent a consolidation if it is authorized by the legislature.<sup>310</sup> But neither the consolidating corporations nor the legislature can deprive them of their remedy in equity to subject the property of the consolidating corporations, respectively, to the satisfaction of their claims.311

As we shall presently see, creditors of a consolidating corporation may, in the absence of provision to the contrary, maintain actions on their claims against the consolidated corporation, if they see fit to do so. 312 But they are entitled, if they choose, to have the assets of the consolidating corporation distributed as in the case of a simple dissolution, and they cannot be compelled to surrender this right, and accept instead the liability of the consolidated corporation, 313 unless there was legislative

v. Marsh, 17 Wis. 13, 1 Cum. Cas. 897; State v. Bailey, 16 Ind. 46, 79 Am. Dec. 405; post, § 482.

307 See Martin v. Pensacola & Georgia R. Co., 8 Fla. 370, 73 Am.

308 Pacific Railroad v. Hughes, 22

Mo. 291, 64 Am. Dec. 265. 309 Sparrow v. Evansville Crawfordsville R. Co., 7 Ind. 369;

Bish v. Johnson, 21 Ind. 299; Mansfield, Coldwater & L. M. R. Co. v. Brown, 26 Ohio St. 233; Edwards v. People, 88 III. 340.

310 People v. Empire Mutual Life Ins. Co., 92 N. Y. 105; Houston & 56 Tex. 609; In re Manchester & fett v. Great Western R. Co., 25 Ill. London Life Assurance & Loan 353; Powell v. North Missouri R. Ass'n, L. R. 9 Eq. 643; post, § 357. Co., 42 Mo. 68. See, also, In re

311 Chicago, Rock Island & Pac. R. Co. v. Moffitt. 75 III. 524; New Bedford R. Co. v. Old Colony R. Co., 120 Mass. 397; post, § 357; and cases in the notes following.

312 Post, § 356. 313 Chicago, Rock Island & Pac. R. Co. v. Moffitt, 75 III. 524; Wabash, St. Louis & Pac. Ry. Co. v. Ham, 114 U.S. 587; New Bedford R. Co. v. Old Colony R. Co., 120 Mass. 397; Warren v. Mobile & Montgomery R. Co., 49 Ala. 582; Market Street Ry. Co. v. Hellman, 109 Cal. 571; Hamilton v. Clarion. Mahoning & P. R. Co., 144 Pa. St. Texas Central R. Co. v. Shirley, 54 34; Smith v. Chesapeake & Ohio Tex. 125; Indianola R. Co. v. Fryer, Canal Co., 14 Pet. (U. S.) 45; Brufauthority for the consolidation at the time they became creditors 314

## § 350. Mode of effecting consolidation under legislative authority.

A statute authorizing two corporations to consolidate does not of itself effect a consolidation, without any action or agreement to that end by the corporations, but merely authorizes them to take proper action to bring about a consolidation.315

If the statute merely confers the power to consolidate, without prescribing any mode of effecting consolidation, the consolidating corporations may agree upon any terms they may see fit, provided they are not unlawful. 316 But in most states the statutes providing for the consolidation of corporations prescribe the steps which shall be taken to bring it about. An illustration from the New York statutes is given in another section. 317 If the statute requires that the consolidation shall be effected in a certain mode or upon certain terms, its provisions must be substantially complied with, except in so far as they may be merely directory, or no consolidation de jure will take place; and, unless they are at least colorably complied with, there will not be even a de facto consolidation.818 Among the steps or formalities which may be re-

Family Endowment Society, 5 Ch. App. 118; Griffith's Case, 6 Ch. App. 374; In re India & London Life Assurance Co., 7 Ch. App. 651; In re Manchester & London Life Assurance & Loan Ass'n, L. R. 9 Eq. 643.

314 Indianola R. Co. v. Fryer, 56 Tex. 609. In this case, authority to consolidate was conferred by the charter of a corporation, and when it afterwards consolidated, it its creditors was against the new corporation.

815 Mason v. Finch, 28 Mich. 282.

817 See ante, § 349(b).

318 Mansfield, Coldwater & L. M. R. Co. v. Drinker, 30 Mich. 124; Tuttle v. Michigan Air Line R. Co., 35 Mich. 247; Peninsular Ry. Co. v. Tharp, 28 Mich. 506; Rodgers v. Wells, 44 Mich. 411; Brown v. Dibble's Estate, 65 Mich. 520; Mansfield, Coldwater & L. M. R. Co. v. Brown, 26 Ohio St. 223; Mansfield, Coldwater & L. M. R. Co. v. Stout. 26 Ohio St. 241.

Where an act authorized corpowas held that the only remedy of rations to consolidate their capital stock, and a supplemental act authorized one of them to purchase the stock of the other in lieu of 316 Dimpfel v. Ohio & Mississippi consolidation of their capital stock, Ry. Co., 9 Biss. 127, Fed. Cas. No. it was held that an actual sale and delivery of its capital stock by the latter to the former was a con-

quired by statutes authorizing consolidation, and which may be conditions precedent, are an agreement between the stockholders of the consolidating corporations, or an agreement between the consolidating corporations, entered into by their boards of directors, and ratified by their stockholders, or a certain proportion of them, at meetings duly called for that purpose; 319 election of a board of directors of the consolidated corporation; 320 filing the agreement or articles of consolidation, or a certified copy thereof, or a certificate of consolidation, in the office of the secretary of state; 321 publishing notice of the in-

Williamson v. New Jersey Southern R. Co., 26 N. J. Eq. 398.

As to de facto consolidation, see

post. § 352.

319 See the Business Corporations Act of New York, referred to, ante, § 349(b). And see Wells v. Rodgers, 60 Mich. 525; Bradford v. Frankfort, St. Louis & T. R. Co., 142 Ind. 383.

As to proof and presumption of ratification of agreement by the stockholders, where the minutes of a consolidating corporation have been lost, see Phinizy v. Augusta & Knoxville R. Co., 62 Fed.

Under a statute authorizing consolidation of corporations when the consent of the holders of "three fourths in value of all the stock of each corporation" is obtained, the word "stock" means stock actually subscribed and outstanding. Market Street Ry. Co.

A statute providing that any railroad corporation in the state may consolidate with a railroad corporation in an adjoining state, "upon such terms as may be by them mutually agreed upon, in accordance with the laws of the adjoining state," does not require that a meeting of the stockholders of a corporation in the state, called to act upon a proposition to consolidate with a corporation in an adjoining state, shall be called and

solidation in accordance with the laws of such adjoining state, but only that the terms of consolidation shall not be in conflict with such laws. Bradford v. Frankfort, St. Louis & T. R. Co., 142 Ind. 383.

The agreement must state matters required by the statute to be stated, as the number and residence of the new directors, etc. State v. Vanderbilt, 37 Ohio St. 590.

A consolidation of corporations is not invalid because the agreement of consolidation has no certificate upon it by the secretaries of the several companies that it has been accepted. Phinizy v. Augusta & Knoxville R. Co., 62 Fed. 678.

Where an agreement of consolidation is duly signed and sealed after the meetings of the stockholders of both companies have been held as required by the statute, and the consolidation has been ordered, it is not invalid because it bears a date prior to such meet-Wells v. Rodgers, 60 Mich. ings. 525.

320 Mansfield, Coldwater & L. M.

R. Co. v. Drinker, 30 Mich. 124.
321 Mansfield, Coldwater & L. M. R. Co. v. Brown, 26 Ohio St. 223; Com. v. Atlantic & Great Western Ry. Co., 53 Pa. St. 9; Peninsular Ry. Co. v. Tharp, 28 Mich. 506; Trester v. Missouri Pacific R. Co., 23 Neb. 171 33 Neb. 171.

Under an act authorizing consolidation of corporations, and proconducted in accordance with the viding that the agreement of contended consolidation, and of meetings for the purpose of an agreement; 322 payment of a fee or tax upon the filing of the agreement or certificate of consolidation in the office of the secretary of state.323

In the absence of evidence to the contrary, it will always be presumed that corporations, in consolidating under statutory authority, have complied with the requirements of the stat-

fice of the secretary of state, and that it should from "thence be deemed the agreement and act of consolidation," it was held that such filing was essential to a valid consolidation. Com. v. Atlantic & Great Western Ry. Co., 53 Pa. St. 9.

Such filing makes the new company a corporation. Id.

Where corporations, however, were consolidated under such a statute, and a subscription was made after the agreement for consolidation, but before the certificate or agreement was filed in the office of the secretary of state, the subscription was held valid. Mc-Clure v. People's Freight Ry. Co., 90 Pa. St. 269.

322 See Tuttle v. Michigan Air Line R. Co., 35 Mich. 247; Wells v. Rodgers, 60 Mich. 525.

Notice will be presumed when the record shows that a majority of the directors were present at the meeting and voted to consolidate, and nothing appears to the contrary, and the burden of showing want of notice is on one who denies the validity of the consolidation. Wells v. Rodgers, 60 Mich. 525.

323 State v. Chicago & Eastern Illinois R. Co., 145 Ind. 229; People v. Rice, 57 Hun, 486, 128-N. Y. 521; Ashley v. Ryan, 49 Ohio St. 504.

A statute requiring payment of a tax on its capital stock, upon the porated by or under any general or cases there cited.

solidation, or a certified copy special law of the state," requires thereof, should be filed in the of-payment of such a tax by a new corporation formed by consolidation of pre-existing corporations, although each of them may have paid such a tax upon its own incorporation. People v. Rice, 57 Hun (N. Y.) 486, 128 N. Y. 591. Compare People v. Rice, 66 Hun, 130, 138 N. Y. 614.

> The state cannot recover the fees or tax unless the agreement or certificate is filed, and it is not filed where the agent of the companies, upon applying to the secretary of state to file the same, and being informed of the amount required to be paid, refuses to pay the same, and carries the papers away with him, with the consent of the secretary of state or his deputy. State v. Chicago & East-ern Illinois R. Co., 145 Ind. 229.

> Under a statute requiring the payment of a fee to the secretary of state for filing articles of incorporation or consolidation, the fee is payable upon the filing of articles of consolidation between a corporation of the state and a corporation or corporations of another state, as well as in the case of consolidation of corporations of the state. Ashley v. Ryan, 49 Ohio St. 504.

There is a conflict of opinion as to whether this is true where the statute requires payment of a fee or tax on the filing of incorporation papers by "every corporation filing of incorporation papers, by incorporated under the laws" of "every corporation \* \* \* incor- the state. See post, § 362(d), and ute.324 And defective consolidation may be cured and rendered perfectly valid by legislative ratification or recognition.325

# Effect of unauthorized or ineffectual attempt to consolidate.

If corporations assume to enter into a consolidation when there is no legislative authority therefor, so that they do not acquire an existence as a consolidated corporation either de jure or de facto, they can neither acquire rights nor incur liabilities as a consolidated company, 326 unless by virtue of the doctrine of equitable estoppel. 327 In such a case, however, they may acquire rights and incur liabilities in their original corporate capacity, by reason of their business and transactions as a consolidated company.328

An ultra vires agreement to consolidate is void, and cannot be enforced by the courts at the suit of either party; and it can make no difference that it has been partly performed. 329

Attempted consolidation not a dissolution.—When corporations attempt to consolidate, but the attempted consolidation is void, and one of them withdraws, there is no dissolution. 330 Indeed,

See ante, § 349(c).

326 Mansfield, Coldwater & L. M. R. Co. v. Brown, 26 Ohio St. 223; Mansfield, Coldwater & L. M. R. Co. v. Stout, 26 Ohio St. 241; Mansfield, Coldwater & L. M. R. Co. v. Drinker, 30 Mich. 124; Tuttle v. Michigan Air Line R. Co., 35 Mich. 247; Brown v. Dibble's Estate, 65 Mich. 520; Peninsular Ry. Co. v. Tharp, 28 Mich. 506.

327 Post, § 353.

328 Where railroad companies undertake to consolidate without authority, and run their lines as a consolidated company, they cannot escape liability for injuries to passengers, loss of baggage, loss of or

324 Swartwout v. Michigan Air ground that the consolidation Line R. Co., 24 Mich. 390; Lewis v. agreement was ultra vires, and City of Clarendon, 5 Dill. 329, Fed. they may be sued jointly therefor. Cas. No. 8,320.

Bissell v. Michigan Southern & 325 McAuley v. Columbus, Chi- Northern Indiana R. Cos., 22 N. Y. Cago & I. C. Ry. Co., 83 Ill. 348. 258, 1 Smith's Cas. 522, 1 Cum. Cas. 187. And see ante, §§ 214(b),

> Where a railroad company has made an ineffectual attempt to consolidate, it is liable for an injury to a passenger caused by the negligence of persons operating the road by virtue of the attempted consolidation. Latham v. Boston, Hoosac Tunnel & W. Ry. Co., 38 Hun (N. Y.) 265.

> 329 Greenville Compress & Warehouse Co. v. Planters' Compress & Warehouse Co., 70 Miss. 669, 35 Am. St. Rep. 681. And see ante, §

330 Chevra Bnai Israel Anshe injury to goods carried, etc., on the Yanove Und Motal v. Chevra Bithis is true, even though there may be no withdrawal.<sup>331</sup> Where a turnpike corporation attempted a consolidation with another, and the consolidation was afterwards held by the courts to be illegal and void, it was held that the company did not cease to be a corporation, or forfeit its corporate property and franchises, because it did not, during the attempted consolidation, keep up its separate organization, and separately exercise its corporate powers.332

#### § 352. De facto corporate existence.

The principles of law with respect to de facto corporate existence, explained at length in a former chapter, 333 apply to a corporation formed by the consolidation of other corporations. If there is valid legislative authority for a consolidation, an attempt in good faith to consolidate under the statute, a colorable compliance with the statute, and exercise or assumption of powers as a consolidated corporation, the new or consolidated corporation is a corporation de facto, and, as a general rule, its corporate existence can only be attacked by the state, and in a direct proceeding.334

kur Cholim Anshe Rodof Sholem, nies were consolidated under law-

24 Misc. Rep. (N. Y.) 189.
331 American Loan & Trust Co.
v. Minnesota & Northwestern R.
Co., 157 Ill. 641, 651. And see Topeka Paper Co. v. Oklahoma Publishing Co., 7 Okla. 220.

332 State v. Crawfordsville & Darlington Turnpike Co., 102 Ind.

600. See ante, § 309.

233 Ante, § 80 et seq. 234 Swartwout v. Michigan Air Line R. Co., 24 Mich. 390; Farm-ers' Loan & Trust Co. v. Toledo, Ann Arbor & N. M. Ry. Co., 67 Fed. 49; Continental Trust Co. v. Toledo, St. Louis & K. C. R. Co., 82 Fed. 642; Chicago, Kansas & W. R. Co. (N. J. Eq.) 10 Atl. 741.

ful authority, it was held that a court of equity had no jurisdiction, upon the application of a bondholder or stockholder in one of the original companies, to put an end to the consolidated company, upon the alleged ground that it had its origin in a fraudulent design, and was created to answer a fraudulent purpose, nor upon the ground that the proceedings for consolidation were defective. Terhune v. Midland R. Co., 38 N. J. Eq. 423.

A bill to annul a consolidation made by several railroad compa-nies, and to have a mortgage executed by the consolidated company R. Co. v. Stafford County Com'rs, on the aggregate property declared 36 Kan. 121; Terhune v. Midland void, on the ground that one of R. Co., 38 N. J. Eq. 423; Bell v. the roads taken into the consolida-Pennsylvania, Slatington & N. E. tion had no legal existence, cannot Co. (N. J. Eq.) 10 Atl. 741. be maintained by stockholders of where several railroad compaIt has been held, however, that a merely de facto consolidated corporation, although it may be entitled to sue on its contracts, cannot enforce a subscription to the stock of one of its constituent corporations, but that, in order to do this, it must show compliance with all the requirements of the statute authorizing the consolidation.<sup>335</sup> And it has been held that if the maker of a note to a corporation is sued thereon by the assignee of another corporation, which is claimed to have succeeded to the rights of the former by consolidation, the regularity of the consolidation must be proved, to show title in the successor.<sup>336</sup>

There is a de facto consolidated corporation where there is an attempt in good faith to consolidate, under a valid law authorizing such a consolidation, although there may have been a failure to give the notice to stockholders, or to file the certificate of consolidation, as required by the statute.<sup>337</sup> But there cannot be a de facto consolidated corporation if there has been no attempt at all to comply with the requirements of the statute, or if there is not at least a colorable compliance therewith.<sup>338</sup>

If there were no decision to the contrary, it would seem clear that there cannot be a *de facto* consolidated corporation, if there is no valid law authorizing the consolidation, for, as we have seen, the great weight of authority is to the effect that, in order that there may be a *de facto* corporation, there must be an apparent right, and therefore there must be some authority of law under which, except for defects and irregularities in organization, there might be a *de jure* corporation. And so it has been held in a late Illinois case. It has been held by

must be instituted, if at all, by the state through its attorney general. Bell v. Pennsylvania, Slatington & N. E. R. Co. (N. J. Ch.) 10 Atl. 741.

335 Mansfield, Coldwater & L. M. R. Co. v. Drinker, 30 Mich. 124; Tuttle v. Michigan Air Line R. Co., 35 Mich. 247; Mansfield, Coldwater & L. M. R. Co. v. Brown, 26 Ohio St. 223; Mansfield, Coldwater & L. M. R. Co. v. Stout, 26 Ohio St. 241. 336 Brown v. Dibble's Estate, 65

Mich. 520.

337 Farmers' Loan & Trust Co. v. Toledo, Ann Arbor & N. M. Ry. Co., 67 Fed. 49; and other cases in note 334, supra.

338 See ante, § 82(f).

339 Ante, § 82(c).

340 American Loan & Trust Co.

a federal court, however, that there is, in such a case, no want of authority for a de jure corporation, but a mere want of capacity in the constituent elements of which the consolidated corporation is formed, and that the consolidated association, therefore, may have a de facto corporate existence, notwithstanding there is no law authorizing the consolidation.<sup>341</sup> This decision cannot be sustained. Its effect is to do away almost altogether with the rule that corporations cannot consolidate without legislative authority, except where the consolidation is attacked in a direct proceeding by the state. To permit corporations to consolidate ad libitum, except as against a direct attack by the state, is not only contrary to law, but is clearly contrary to public policy.

#### Estoppel to deny validity of consolidation. § 353.

Corporations formed by consolidation of other corporations are within the protection of, and subject to, the doctrine under which corporations and persons are held to be estopped, under certain circumstances, from denying corporate existence.342 Thus it has been held that when railroad corporations have undertaken to consolidate, a county or city which afterwards subscribes to the capital stock of the new corporation, and issues its bonds in payment of the subscription, is thereby estopped to deny the validity of the consolidation or the legal existence of the new corporation.343

v. Minnesota & Northwestern R. Co., 157 Ill. 641, 651. It was held in this case that, where corporations attempt to consolidate with-ledo, St. Louis & K. C. R. Co., 82 out any authority, they do not become a de facto consolidated corporation, since there cannot be a de facto corporation unless there Dill. 329, Fed. Cas. No. 8,320; a law authorizing such a corpo-Young v. Township of Clarendon, ration, and that contracts made by 26 Fed. 805. See, also, Swartwout such a supposed consolidated comv. Michigan Air Line R. Co., 24 pany are invalid. It was further Mich. 390; Dimpfel v. Ohio & Misheld that such a contract is not enforceable against one of the original companies unless there is & Knoxville R. Co., 62 Fed. 678.

something to show that it made or authorized the contract.

Fed. 642.

342 Ante, § 83 et seq. 343 Lewis v. City of Clarendon, 5

The fact that a consolidation between two railroad companies or other corporations is ultra vires cannot be set up by them as a defense to escape liability on a contract made by them after the consolidation, and for which they have received the consideration, or to escape liability for torts committed by them in their operations under the consolidation agreement.344 And where corporations undertake to consolidate, the stockholders consenting, and, as a consolidated corporation, issue bonds secured by a mortgage, both the consolidated corporation and the stockholders are estopped, as against the holders of the bonds, to attack the consolidation as invalid.345

Where corporations undertake to consolidate, and issue mortgage bonds, a general creditor whose claim is based upon a contract made with it as a consolidated corporation cannot question the validity of the consolidation for the purpose of attacking the bonds and mortgage.346

A corporation which has, in effect, consolidated with another is estopped to assert that the proceedings for consolidation were. not in accordance with the terms of the statute, in an action against it to recover the amount of a judgment against the other corporation on the ground that there has been a consolidation.347

When stockholders of a corporation consent to its consolidation, under a statute, with another corporation, and the new corporation contracts debts, they cannot attack the statute under which they consolidated as unconstitutional, for the purpose of escaping individual liability for such debts, imposed by a constitutional or statutory provision adopted or enacted prior to the consolidation.348

<sup>345</sup> Farmers' Loan & Trust Co. v. Toledo, Ann Arbor & N. M. Ry. Co. v. Ashling, 160 Ill. 373. Co., 67 Fed. 49.

<sup>344</sup> Bissell v. Michigan Southern ville, New Albany & C. Ry. Co. (C. & Northern Indiana R. Cos., 22 N. C A.) 84 Fed. 539. And see Con-Y. 258, 1 Smith's Cas. 522, 1 Cum. tinental Trust Co. v. Toledo, St. Cas. 187. Louis & K. C. R. Co., 82 Fed. 642.

<sup>347</sup> Chicago, Santa Fe & C. Ry.

<sup>348</sup> Gardner v. Minneapolis & St. 346 Louisville Trust Co. v. Louis- Louis Ry. Co., 73 Minn. 517.

### § 354. Dissolution of consolidating corporations, and creation of new corporation.

Since the rights of the parties will vary according to the effect of a consolidation upon the consolidating corporations, it is often important to determine whether a consolidation has the effect of dissolving the consolidating corporations, and creating a new corporation as of the time of the consolidation, or whether it merely continues the existence of one of them, and dissolves the others, or whether it dissolves any of them.

Creation of new corporation.—Ordinarily, when corporations are consolidated under legislative authority, all of the consolidating corporations are dissolved and extinguished absolutely, so that they no longer exist for any purpose, and an entirely new and distinct corporation is created, as of the time of the consolidation, with the combined rights, franchises, privileges, and property of the consolidating corporations.349

Merger in corporation, the existence of which is continued.— This, however, is not necessarily the case. Whether a consolidation has this effect in any particular case depends upon the intention. As was stated in defining consolidation in a for-

Wall. (U.S.) 25; Shields v. Ohio, 95 V. S. 319; Atlantic & Gulf R. Co. Co. v. Hobart, 2 Gray (Mass.) 543; v. Georgia, 98 U. S. 359, 1 Keener's Cheraw & Salisbury R. Co. v. Comcas. 107; Keokuk & Western R. missioners of Anson, 88 N. C. 519; Co. v. Missouri, 152 U. S. 301; Com. v. Atlantic & Great Western Ridgway Township v. Griswold, 1 Ry. Co., 53 Pa. St. 9; Marquette, McCrary, 151, Fed. Cas. No. 11,819; Houghton & Ontonagon R. Co. v. State v. Bailey, 16 Ind. 46, 79 Am. Langton, 32 Mich. 251; People v. Dec. 405; McMahan v. Morrison, Louisville & Nashville R. Co., 120 16 Ind. 172, 79 Am. Dec. 418; Peo- Ill. 48; Ohio & Mississippi Ry. Co. ple v. New York, Chicago & St. L. v. People, 123 Ill. 467; Crawfords-R. Co., 129 N. Y. 474, 1 Keener's ville & Southwestern Turnpike Co. 'Cas. 129; Gardner v. Minneapolis v. Fletcher, 104 Ind. 97; Charlotte, & St. Louis Ry. Co., 73 Minn. 517; Kansas, Oklahoma & T. Ry. Co. v. Co., 35 La. Ann. 413; Board of Ad- Co., 77 Miss. 194. ministrators of Charity Hospital v. New Orleans Gas Light Co., 40 La. See, also, St. Louis, Iron Moun-Ann. 382; Day v. Worcester, tain & S. Ry. Co. v. Berry, 41 Ark.

349 Clearwater v. Meredith, 1 Nashua & Rochester R. Co., 151 all. (U. S.) 25; Shields v. Ohio, 95 Mass. 302; Hamilton Mutual Ins. Columbus & A. R. Co. v. Gibbes, 27 S. C. 385; State v. Le Sueur, 145 Smith, 40 Kan. 192; State v. Maine Mo. 322; Rio Grande Western Ry. Central R. Co., 66 Me. 488; Maine Co. v. Telluride Power & Trans-Central R. Co. v. Maine, 96 U. S. mission Co., 16 Utah, 125; Adams 499; Fee v. New Orleans Gas Light v. Yazoo & Mississippi Valley R.

mer section, 350 the legislature may authorize a consolidation by the merger of one existing corporation in another, and continue the existence of the latter with the rights, franchises, privileges, and property of the former, in addition to its own. If such an intention appears, the merging corporation only is dissolved.351 The fact that the name of the continuing corporation is changed does not tend to show that it is a new corporation, for a change in the name of a corporation works no change in its identity.352

Where an act of the legislature authorized two railroad companies (A, and B.) to unite and consolidate their stocks, and all their rights, privileges, immunities, property, and franchises, under the name and charter of A., in such manner that each owner of shares of the stock of B. should be entitled to receive an equal number of shares of the consolidated company, and declared that all contracts of both companies should be assumed by and be binding upon A.; that its capital stock should not exceed the aggregate of the capital stock of both companies; that all their benefits and rights should accrue to it; and that, upon the union and consolidation, each stockholder of B. should be entitled to receive a certificate for a like number of shares of stock of A. upon surrender of his certificate of stock of B.,-it was held that the consolidation did not dissolve both A. and B., and create a new company, but dissolved B. only, merging it in A.353

A contract of consolidation, whereby one corporation transfers all of its property and franchises to another, under legis-

<sup>509;</sup> Market Street Ry. Co. v. Hellman, 109 Cal. 571.

<sup>350</sup> Ante, § 348. 351 Central Railroad & Banking Co. v. Georgia, 92 U. S. 665, 1 Keener's Cas. 96; Atlantic & Gulf R. Co. v. Georgia, 98 U. S. 359, 1 Keener's Cas. 107; Philadelphia, Wilming-ton & B. R. Co. v. Maryland, 10 preceding. And see ante, § 339(g). How. (U. S.) 376; Booe v. Junction R. Co., 10 Ind. 93; Meyer v. Co. v. Georgia, 92 U. S. 665, 1 Johnston, 64 Ala. 603; Chicago, Keener's Cas. 96.

Santa Fe & C. Ry. Co. v. Ashling, Santa Fe & C. Ry. Co. v. Asning, 160 III. 373; Bishop v. Brainerd, 28 Conn. 289; Berry v. Kansas City, Ft. Scott & M. R. Co., 52 Kan. 759, 39 Am. St. Rep. 371, 52 Kan. 774, 39 Am. St. Rep. 381.

<sup>352</sup> Meyer v. Johnston, 64 Ala.

lative authority, is, unless a contrary intention appears, a surrender of its charter by the former with the consent of the state, and operates as a dissolution of that corporation, but the existence of the corporation to which the transfer is made continues.<sup>354</sup>

Continuance of both corporations.—Sometimes a statute authorizing consolidation, while it does not provide for continuance of the consolidating corporations for all purposes, or indefinitely, expressly provides for their continuance for certain purposes, as for the purpose of adjusting their liabilities, or transferring their property.<sup>355</sup>

It is undoubtedly within the power of the legislature to provide for a combination of corporations without the dissolution of either of them, and it might call the combination a consolidation. The term "consolidation," however, cannot properly be applied to such a combination, unless it is so applied by the legislature, for the term signifies "the act of bringing together and uniting several particulars, details, or parts into one body or whole," 356 and if two corporations enter into a combination, in which each continues its separate existence, there is not one body or whole, but two separate and distinct bodies.

# § 355. Rights, powers, franchises, privileges, and property of consolidated corporation.

(a) In general.—When corporations are consolidated, the rights, franchises, and privileges of the consolidated corporation depend upon the intention of the legislature as manifested by the statute authorizing the consolidation. The legislature may

354 Lauman v. Lebanon Valley R. Co., 30 Pa. St. 42, 72 Am. Dec. 685; Chicago, Santa Fe & C. Ry. Co. v. Ashling, 160 III. 373; Chicago & Eastern Illinois R. Co. v. State, 153 Ind. 134.

855 Lightner v. Boston & Albany post, §§ 355 R. Co., 1 Lowell, 338, Fed. Cas. No. 8,343; Whipple v. Union Pacific Ry. Co., 28 Kan. 474; Baltimore & solidation."

Susquehanna R. Co. v. Musselman, 2 Grant's Cas. (Pa.) 348; East Tennessee & Georgia R. Co. v. Evans, 6 Heisk. (Tenn.) 607; Edison Electric Light Co. v. New Haven Electric Co., 35 Fed. 233. See post, §§ 355(b), note 377, 356(e).

856 Century Dict. & Cyc. "Consolidation."

confer upon it, with the consent of the consolidating corporations, which consent is given impliedly by entering into the consolidation, all the rights, franchises, privileges, and property of the consolidating corporations, or it may withhold some of them, or it may add to them new rights, franchises, or privileges. A consolidated corporation has such powers only as are expressly or impliedly conferred by the statute authorizing the consolidation.857

If there is no provision to the contrary in the statute or the agreement between the parties, the general rule, based upon the presumed intention of the legislature and the corporations, is that the consolidated corporation acquires by the consolidation all the rights, franchises, privileges, and property of the consolidating corporations, subject to the same burdens and restrictions which attached thereto in the hands of the consolidating corporations, respectively, under their charters.358

66 Me. 488, and cases cited in the

notes following.

358 Philadelphia, Wilmington & B. R. Co. v. Maryland, 10 How. (U. S.) 376; Tomlinson v. Branch, 15 Wall. (U. S.) 460; Nugent v. Supervisors, 19 Wall. (U. S.) 249; Central Railroad & Banking Co. v. Georgia, 92 U.S. 665, 1 Keener's Cas. 96; Branch v. City of Charleston, 92 U. S. 677; Maine Central R. Co. v. Maine, 96 U. S. 499; Green County v. Conness, 109 U.S. 104; New Orleans Gas Light Co. v. New Orleans Gas Light Co. v. New Orleans Light & Heat Producing & Mfg. Co., 115 U. S. 650; Lightner v. Boston & Albany R. Co., 1 Lowell, 338, Fed. Cas. No. 8,343; Lewis v. City of Clarendon, 5 Dill. 329, Fed. Cas. No. 8,320; Zimmer State 20 Arts C77, Mod r. mer v. State, 30 Ark. 677; Mead v. New York, Housatonic & N. R. Co., 45 Conn. 199; Bishop v. Brainerd, 28 Conn. 289; Robertson v. City of Rockford, 21 Ill. 451; Cooper v. Corbin, 105 Ill. 224, 231; Hubbard v. Chappel, 14 Ind. 601; Paine v.

357 State v. Maine Central R. Co., 939, 30 Am. St. Rep. 599; Trester v. Missouri Pacific R. Co., 33 Neb. 171; Rome, Watertown & O. R. Co. v. Ontario Southern R. Co., 16 Hun (N. Y.) 445; Fisher v. New York Central & Hudson River R. Co., 46 N. Y. 644; South Carolina R. Co. v. Blake, 9 Rich. Law (S. C.) 228; Lancaster. Miller v. (Tenn.) 514.

As to the rights of a consolidated railroad company under proceedings to condemn land instituted by one of the consolidating companies, see post, § 361, note

Where a railroad company is consolidated with another under statutory authority, its land vests in the consolidated company. Cashman v. Brownlee, 128 Ind. 266.

Where two boom companies, each being required by its charter to maintain a boom sufficiently strong to retain all the lumber contained in it, were consolidated under a statute giving the consolidated company all the rights and Lake Erie & Louisville R. Co., 31 privileges, and subjecting it to all Ind. 283; Louisville, New Orleans the restrictions, of the charters of & Texas Rv. Co. v. Blythe, 69 Miss. the consolidating companies, it erally, there is an express provision to this effect in the statute authorizing consolidation, but it is not at all necessary. Such an intention on the part of the legislature will be presumed in the absence of provision to the contrary.<sup>359</sup> When corporations "unite or become consolidated under authority of law, the presumption is, until the contrary appears, that the united or consolidated company has all the powers and privileges, and is subject to all the restrictions and liabilities, of those out of which it was created." <sup>360</sup>

It was held in a Maine case that, when a new corporation is formed by the consolidation of existing corporations, and by the act authorizing the consolidation, the new corporation is to have the powers, privileges, and immunities possessed by "each" of the consolidating corporations, the new corporation will have only the powers, privileges, and immunities which the corporation with the fewest powers, privileges, and immunities possessed, and which were common to all. It may well be doubted, however, whether this was the intention of the legislature. 362

Under a provision giving a consolidated corporation the rights, franchises, privileges, and property of the consolidating corporations, or without such a provision, and in the absence of provision to the contrary, it has been held that a consolidat-

was held that the consolidated company was not bound to maintain the lower boom sufficient to retain all the lumber which might be carried away from the upper boom by the act of God, but was only required to maintain it sufficient to retain all logs intended for it. "The effect of the consolidation," said the court, "was to unite the companies only, not the booms; the consolidated company controlled each of them separately, 'under the rights, privileges and immunities,' and 'subject to the restrictions, contained in the respective charters.' Brown v. Susquehanna Boom Co., 109 Pa. St. 57, 58 Am. Rep. 708; Gould v. Langdon, 43 Pa. St. 365.

A corporation formed by an authorized consolidation of two or more corporations holds its property acquired by the consolidation in its own right, and not in trust for the constituent companies, even when it is liable for the debts of the latter. Greene v. Woodland Avenue & West Side Street R. Co., 62 Ohio St. 67.

359 See the cases cited in the note preceding.

360 Chief Justice Waite, in Tennessee v. Whitworth, 117 U. S. 139, 147

361 State v. Maine Central R. Co., 66 Me. 488.

362 See the cases in note 358, supra, and in the notes following.

ed corporation acquired the power of eminent domain enjoyed by one or both of the consolidating corporations;363 the right, in the case of a railroad company, to charge a certain rate for transportation of persons or property;364 the power, though a quasi public corporation, like a railroad company, to mortgage its property and franchises;365 an immunity of officers and employes from working on the public roads or serving on the jury;366 the right to compromise and settle a claim against one of the consolidating corporations, and to maintain an action to enforce a settlement;367 the right to the benefit of a license to use a patent enjoyed by the consolidating corporations;368 and the right (in case of a railroad company, for example) to receive subscriptions by cities and other municipalities to its capital stock, payable in bonds of the municipality.369

When the effect of a consolidation of corporations is to dissolve the old corporations and create an entirely new corporation, the powers and franchises of the new corporation are determined by the law in force at the time of the consolidation.370

When consolidating corporations are dissolved by the consolidation, and thereby incapacitated from performing duties to the public, in consideration of the performance of which

363 South Carolina R. Co. v. Blake, 9 Rich. Law (S. C.) 228; Trester v. Missouri Pacific R. Co., 33 Neb. 171.

364 Fisher v. New York Central & Hudson River R. Co., 46 N. Y. 644.

365 Mead v. New York, Housatonic & N. R. Co., 45 Conn. 199.

366 A provision in the charter of a railroad company exempting its officers, agents, and servants from military and road duty, and service on juries, is not a mere personal privilege conferred upon the class of persons described, but consti- See infra, this section, (f).

tutes a valuable right of the corporation, and passes to a new corporation formed by consolidation of such corporation with another. Zimmer v. State, 30 Ark. 677.

367 Paine v. Lake Erie & Louisville R. Co., 31 Ind. 283.

368 Lightner v. Boston & Albany R. Co., 1 Lowell, 338, Fed. Cas. No. 8,343. See, also, Ridgway Township v. Griswold, 1 McCrary, 151, Fed. Cas. No. 11,819.

369 Lewis v. City of Clarendon, 5 Dill. 329, Fed. Cas. No. 8,320. 370 Shields v. Ohio, 95 U. S. 319. they were granted exemptions by their charters, the exemptions cease.371

(b) Contracts and claims of consolidating corporations.—Generally, by express provision of the statute or agreement of consolidation, and by implication, in the absence of provision to the contrary, the consolidated corporation succeeds to and may enforce the rights of the consolidating corporations under contracts made by them; before the consolidation.<sup>372</sup> Debtors of the original corporations are no longer indebted to them, but become the debtors of the new corporation.<sup>373</sup> But to entitle a consolidated corporation to enforce contracts made by the consolidating corporations, it must show at least a colorable compliance with all the requirements of the law authorizing the consolidation.374

Where a statute authorizes corporations to consolidate, or consolidates them, and vests all their property in the consolidated corporation, including choses in action, the consolidated corporation may sue in its own name on choses in action of the consolidating corporations, although such right may not be given in express terms. 375

Where railroad corporations were consolidated under a statute providing that the consolidated corporation should possess all the rights theretofore vested in the old corporations, and that all their property and rights of action should be deemed to be transferred to it, it was held that the consolidated corporation could recover on an indemnity bond given by

Maine, 96 U.S. 499.

<sup>372</sup> Brown v. Dibble's Estate, 65 Mich. 520; Lightner v. Boston & Albany R. Co., 1 Lowell, 338, Fed. Cas. No. 8,343.

<sup>373</sup> Bishop v. Brainerd, 28 Conn.

Where railroad companies were consolidated under an act which vested in the consolidated corporation all the powers, rights, franit was held that the consolidated ter's Estate, 42 Vt. 99.

<sup>371</sup> Maine Central R. Co. v. corporation had the right to use a patented axle-box which both of the old corporations had been licensed to use. Lightner v. Boston & Albany R. Co., 1 Lowell, 338, Fed. Cas. No. 8,343.

<sup>374</sup> Brown v. Dibble's Estate, 65 Mich. 520; Mansfield, Coldwater & L. M. R. Co. v. Drinker, 30 Mich. 124; Tuttle v. Michigan Air Line R. Co., 35 Mich. 247.

<sup>375</sup> University of Vermont & chises, etc., of the old corporations, State Agricultural College v. Bax-

a passenger agent to one of the old companies, its attorney, successors, or assigns, prior to the consolidation, where the agent retained his position, and performed substantially the same duties as formerly.376

The rule that the consolidated corporation acquires all the contract rights of the consolidating corporations only applies to rights acquired by the latter before the consolidation. Where articles of consolidation stipulate that the constituent corporations shall continue in existence for the purpose of settling their liabilities, the new corporation cannot maintain an action on notes indorsed to one of the constituent corporations, without showing ownership of the notes.377

- (c) Subscriptions to stock.—Unless subscribers to the capital stock of a corporation are released from liability on their subscription by the consolidation of the corporation with another, as elsewhere explained, the consolidated corporation succeeds to the rights of the consolidating corporation under the subscriptions, and may enforce the same, provided it shows compliance with all the requirements of the law authorizing the consolidation, but not otherwise.378
- (d) Municipal aid bonds and subscriptions.—When a municipal corporation has not only voted to issue bonds, under legislative authority, in aid of a railroad company, or has voted a subscription to its stock payable in bonds, but has also issued the bonds, the right to the bonds will clearly pass, upon the consolidation of the corporation with another, to the consolidated company. Even when the consolidation is effected before the bonds are issued, but after the municipality

121.

377 Union Pacific Ry. Co. v. Gochenour, 56 Kan. 543.

R. Co. v. Drinker, 30 Mich. 124; Co., 7 Ind. 369; Bish v. Johnson, 21 Tuttle v. Michigan Air Line R. Co., Ind. 299.

35 Mich. 247; Mansfield, Coldwater & L. M. R. Co. v. Brown, 26 Ohio leases subscribers, see post, § 482.

876 Pennsylvania & Northwest-St. 223; Mansfield, Coldwater & L. ern R. Co. v. Harkins, 149 Pa. St. M. R. Co. v. Stout, 26 Ohio St. 241; Sprague v. Illinois River R. Co., 19 Ill. 177; Hanna v. Cincinnati & Ft. Wayne R. Co., 20 Ind. 30; Sparrow 378 Mansfield, Coldwater & L. M. v. Evansville & Crawfordsville R.

has voted the appropriation or subscription, the right to the bonds will vest in the consolidated corporation, if the consolidation was authorized by the charter of the corporation, or by a general law in force at the time of the vote.<sup>379</sup> er the same rule applies when the consolidation was not authorized at the time of the vote is doubtful, and the authorities on the question are not in accord.380

(e) Exemption from taxation.—When corporations which enjoy an exemption from taxation are consolidated under legislative authority, and a new corporation is created, and vested with all the property, rights, franchises, and privileges of the consolidating corporations, the new corporation cannot acquire an exemption from taxation, whatever may be the intention of the legislature, if, at the time of the consolidation, there is a constitutional prohibition against exemptions from taxation. And it can make no difference that the prohibition was not in force at the time the exemption was granted to the consolidating corporations.381

When there is no constitutional prohibition in the way, whether an exemption enjoyed by the old corporations passes to the consolidated corporation depends upon the intention of the legislature. It passes if the legislature so intends and provides, but not otherwise.382 As has been shown in an-

379 Nugent v. Supervisors, 19 Wall. (U. S.) 241; New Buffalo v. B. R. Co. v. Maryland, 10 How. (U. Iron Co., 105 U. S. 73; Chickaming S.) 376; Tennessee v. Whitworth, v. Carpenter, 106 U. S. 663; Bates 117 U. S. 129, 139; State v. Keccounty v. Winters, 112 U. S. 325; kuk & Western R. Co., 99 Mo. Wilson v. Salamanca, 99 U. S. 499; Harter v. Kernochan, 103 U. S. 562; Scott v. Hansheer, 94 Ind. 1; Edwards v. People, 88 Ill. 340.

380 See the cases above cited.

381 Memphis & Little Rock R. Co. v. Railroad Commissioners, 112 U. S. 609; St. Louis, Iron Mountain & S. Ry. Co. v. Berry, 113 U. S. 465; Chesapeake & Ohio Ry. Co. v. Miller, 114 U. S. 176.

section, (f).

382 Philadelphia, Wilmington & 30; Keokuk & Western R. Co. v. Scotland County Court, 41 Fed. 305; Atlanta & Richmond Air-Line R. Co. v. State, 63 Ga. 483; City of Petersburg v. Petersburg R. Co., 29 Grat. (Va.) 773; State v. Philadelphia, Wilmington & B. R. Co., 45 Md. 361, 24 Am. Rep. 511; Natchez, Jackson & C. R. Co. v. Lambert, 70 Miss. 779; Louisville, New Orleans & T. Ry. Co. v. Taylor, 68 Miss. 361; Arkansas Midland R. See ante, § 299(b)(1); infra, this Co. v. Berry, 44 Ark. 17; Com. v. ction, (f).

Nashville, Chattanooga & St. L. R. other chapter, a statute is to be strictly construed in favor of the public, and against the corporation, in determining whether an exemption from taxation is thereby transferred to it from another corporation. And it has been held that a statutory provision that a corporation succeeding to the rights, franchises, and property of another corporation shall have all the rights, franchises, privileges, and immunities enjoyed by the latter, is not to be construed as including an exemption from taxation, unless there is something else to show such an intention on the part of the legislature.<sup>383</sup>

When corporations are consolidated by merger of one in the other, without dissolution of the latter,<sup>384</sup> the latter does not thereby lose an exemption of its property from taxation, granted by its charter, but, as we shall see in a subsequent paragraph, the exemption does not attach to the property and franchises acquired by it from the other corporation.<sup>385</sup>

When two corporations, whose capital stock is by statute exempted from taxation, consolidate themselves into a new corporation under a statute which makes no provision to the contrary, and issue shares in the new company in exchange for shares in the old companies, the right of exemption from taxation attaches to the new shares. It has also been held that when two railroad companies whose capital stock is exempted by statute from taxation within the state, and a third corporation created under the laws of another state, and whose road is in the latter state, consolidate into a new company, and issue shares in the new company in exchange for the shares in the old companies, the right of exemption from taxation in the first state passes into the new shares, unless a law of the first state makes provision to the contrary. 387

Co., 93 Ky. 430; ante, §§ 299(b)(8), Co. v. Georgia, 92 U. S. 665, 1 341(f). Keener's Cas. 96.

<sup>383</sup> Phoenix Fire & Marine Ins.
Co. v. Tennessee, 161 U. S. 174;
ante, § 299(b)(8).

<sup>384</sup> Ante, § 354.
387 Tennessee v. Whitworth, 117
385 Central Railroad & Banking U. S. 139.

When two or more corporations, with a special immunity from general taxation, the amount of taxation being dependent upon certain precedent acts to be done by such corporations, are consolidated into a new corporation, and the new corporation is neither required nor able to do the acts which are to precede such immunity from taxation, the new corporation cannot claim such immunity.388

(f) Effect of constitutional limitations and provisions.—When the charter of a corporation confers upon it a special immunity or privilege, and also authorizes it to consolidate with any other similar corporation, and it enters into such a consolidation, the special immunity or privilege will pass to the new corporation, notwithstanding a constitutional prohibition against the grant of special privileges or immunities adopted by the people before the consolidation, but after the charter of the consolidating corporation.389

But when the authority to consolidate is conferred upon corporations after the adoption of a constitutional provision prohibiting the legislature from granting special privileges or exemptions, or a particular exemption, as an exemption from taxation, for example, or where the authority to consolidate is conferred by a general law, but is not acted upon before the adoption of such a constitutional prohibition, the consolidated corporation, if an entirely new corporation, cannot be given a special privilege or exemption enjoyed by one of the consolidating corporations. 390

having the power under its charter to consolidate with any other railconstitutional prohibition against 609; Chesapeake & Ohio Ry. Co. v. the granting by the legislature of Miller, 114 U. S. 176. See, also, special privileges and immunities. Louisville & Nashville R. Co. v. It was held, notwithstanding such prohibition, that the consolidated ante, § 299(b)(1).

288 State v. Maine Central R. corporation acquired an immunity Co., 66 Me. 488; Maine Central R. of officers and employes from road Co. v. Maine, 96 U. S. 499. and jury service, which was enjoy-389 Zimmer v. State, 30 Ark. 677. ed by the consolidating corpora-In this case, a railroad company tion under its charter.

390 St. Louis, Iron Mountain & road company consolidated with S. Ry. Co. v. Berry, 113 U. S. 465; another company after the adop- Memphis & Little Rock R. Co. v. tion by the people of the state of a Railroad Commissioners, 112 U.S.

When a consolidation results in the creation of a new corporation as of the time of the consolidation, the consolidated corporation becomes subject to a constitutional provision in force at the time of the consolidation, imposing an individual liability upon stockholders of corporations.391

- (g) Effect of reservation of power to alter, amend, or repeal charters.—When corporations which enjoy special privileges or exemptions are consolidated under legislative authority, and a new corporation is created, and the consolidating corporations dissolved, the consolidated corporation is subject to a constitutional provision or a general law adopted or enacted after the creation of the consolidating corporations, but before the grant of authority to consolidate, reserving to the legislature the right to alter, amend, or repeal charters, or withdraw franchises and privileges, subsequently granted, and, therefore, any privileges and exemptions enjoyed by the consolidating corporations, and passing to the consolidated corporation, are subject to such reservation of power.392
- (h) Privilege or exemption enjoyed by one corporation only.— When a consolidated corporation acquires, by express provision or by implication, a special privilege or exemption which attached to the property of one only of the consolidating corporations acquired by it, the privilege or exemption is restricted to that property, and does not exist, in the absence of express provision therefor, with respect to the property derived from the other consolidating corporation, and as to which, in its hands, there was no such privilege or exemption. This rule has been applied to exemptions from taxation, but is equally applicable to other special privileges or exemptions.393 If one of the consolidating corporations has no ex-

Cas. 107. It was so held in this 66 Me. 488. And see ante, § 273(c). case with regard to an exemption from taxation, but the rule also ap-B. R. Co. v. Maryland, 10 How. (U.

391 Gardner v. Minneapolis & St. plies in other cases. See, also, Louis Ry. Co., 73 Minn. 517. Shields v. Ohio, 95 U. S. 319; Maine 392 Atlantic & Gulf R. Co. v. Central R. Co. v. Maine, 96 U. S. Georgia, 98 U. S. 359, 1 Keener's 499; State v. Maine Central R. Co.,

emption from taxation, the property derived from it is not exempt in the hands of the new corporation unless the legislature expressly so provides, although the other consolidating corporation or corporations may have had such an exemption, and although the statutes authorizing the consolidation may give the new corporation all the rights, property, and privileges of the old corporations. The effect is merely to give the new corporation such rights and privileges with respect to the property owned by each one of the old companies as were enjoyed by that particular company under its charter. 394

Thus, where several railroad companies chartered by different states were consolidated under authority from the legislatures of the several states, and the corporation created by one of the states had no exemption from taxation, it was held that the new corporation had no exemption in that state, although one of the other companies, created by another state, enjoyed such an exemption.395 And where a corporation which had no exemption from taxation was merged in another corporation of the same state, which had such an exemption, under a statute giving the latter company all the rights, property, and privileges of the former, it was held that no exemption from taxation attached to the property of the former in the hands of the latter, in the absence of express provision to that effect 396

ing Co. v. Georgia, 92 U. S. 665, 1 Keener's Cas. 96.

394 Philadelphia, Wilmington & B. R. Co. v. Maryland, 10 How. (U. S.) 376; Central Railroad & Banking Co. v. Georgia, 92 U. S. 665, 1 Keener's Cas. 96; Tomlinson v. Branch, 15 Wall. (U. S.) 460; The Delaware Railroad Tax, 18 Wall. (U. S.) 206; Chesapeake & Ohio R. Co. v. Virginia, 94 U. S. 718.

395 Philadelphia, Wilmington &

B. R. Co. v. Maryland, 10 How. (U. S.) 376.

railroad company were consoli-

S.) 376; Central Railroad & Bank- dated under acts of the Maryland and Delaware legislatures providing that the consolidated corporation should have all the rights, powers, and privileges vested in the original companies. It was held that a provision in the charter of the Maryland company exempting the shares of its capital stock from taxation only applied to taxation in Maryland (the charter of the Delaware corporation containing no such exemption), and that the shares of the consolidated company were not exempt from tax-In a later case, a Maryland railation in Delaware. The Delaware road company and a Delaware Railroad Tax, 18 Wall. U. S.) 206. 396 Chesapeake & Ohio R. Co. v.

#### § 356. Burdens and liabilities of consolidated corporation.

(a) In general.—Subject to constitutional limitations, the legislature undoubtedly has the power, in conferring upon corporations authority to consolidate, to impose upon the consolidated corporation, not only all the burdens and all the liabilities which were imposed upon or existed against the consolidating corporations, but also new burdens and liabilities, and if the authority to consolidate is accepted and acted upon, the burdens and liabilities imposed by the statute will attach. On the other hand, the legislature may expressly relieve the consolidated corporation of burdens and liabilities to which the consolidating corporations were subject, provided no constitutional restriction is violated.

In the absence of any express provision in this respect, the general rule is that, where corporations are consolidated under legislative authority, and the consolidated corporation takes the property and franchises of the consolidating corporations, it takes the same subject to precisely the same burdens whick attached to it under the charters of the consolidating corporations respectively.397 Thus, if railroad companies are consolidated, the consolidated corporation takes the property of each of the original companies, in the absence of provision to the contrary, subject to a restriction in its charter as to the rate chargeable for transportation.398 In like manner, in the absence of provisions to the contrary, the duties imposed upon the consolidating corporations by their charters attach to the consolidated corporation.399

cases in note 394, supra. 397 Philadelphia, Wilmington & B. R. Co. v. Maryland, 10 How. (U. S.) 376; The Delaware Railroad Co., 23 Ohio St. 168.

Tax, 18 Wall. 206; Central Railroad & Banking Co. v. Georgia, 92 cinnati R. Co., 23 Ohio St. 168. U. S. 665, 1 Keener's Cas. 96; 399 Pullman's Palace Car Co. v. Chesapeake & Ohio R. Co. v. Virginia, 94 U. S. 718; Board of Ad. 587; Peoria & Rock Island Ry. Co.

Virginia, 94 U. S. 718, and other Ann. 382; United Railroad & Canal Co. v. Commissioner of Railroad Taxation, 37 N. J. Law, 240; Campbell v. Marietta & Cincinnati R. Co., 23 Ohio St. 168.

ministrators of Charity Hospital v. v. Coal Valley Mining Co., 68 Ill. New Orleans Gas Light Co., 40 La. 489; Western Union R. Co. v.

(b) Liability on contracts and for debts of consolidating corporations—(1) In general.—It is undoubtedly within the power of the legislature, in conferring upon corporations authority to consolidate, to make the consolidated corporation liable on all the contracts of the consolidating corporations, and such liability is often imposed in express terms in statutes authorizing consolidation. 400 On the other hand, the legislature may provide that the consolidated corporation shall not be liable on the contracts of the consolidating corporations, or that it shall be liable to a certain extent only,401 though it cannot constitutionally deprive creditors of a consolidating corporation of the right to have a distribution of its property for the satisfaction of their claims,402 and to follow and subject it in equity in the hands of the consolidated corporation.

The difficulty in this connection has been in determining the liability of the consolidated corporation where the legislature has made no express provision in regard thereto, and where there has been no express assumption of liability. In such case, according to the decided weight of authority, the consolidated corporation, if it takes the property of the consolidating corporations, impliedly assumes all their contract liabilities, express or implied, and may be sued thereon. 403

Upon the consolidation of gas companies under a Louisiana statute, it was held that an obligation imposed upon one of them by its charter, to furnish gas free of charge to a certain hospital, be-

Smith, 75 Ill. 496; Gould v. Lang- Ham, 114 U. S. 587. See post, § don, 43 Pa. St. 365.

403 Mt. Pleasant v. Beckwith, 100 U. S. 519; Pullman's Palace Car Co. v. Missouri Pacific Ry. Co., 115 U. S. 587; Continental Trust Co. v. Toledo, St. Louis & K. C. R. Co., 86 Fed. 929; Harrison v. Arkansas came an obligation of the new com-Valley Ry. Co., 4 McCrary, 264, 13 pany. Board of Administrators of Fed. 522; Warren v. Mobile & Gas Light Co., 40 La. Ann. 382.

400 See infra, this section, (2).

See infra, this section, (2). 400 See infra, this section, (2).
401 See Whipple v. Union Pacific
T. R. Co., 37 Ark. 23; Montgomery Ry. Co., 28 Kan. 474; Shaw v. Nor- & West Point R. Co. v. Boring, 51 folk County R. Co., 16 Gray Ga. 582; Western Union R. Co. v. (Mass.) 407, 410. (Mass.) 407, 410. Smith, 75 Ill. 496; Chicago, Rock 402 Chicago, Rock Island & Pac. Island & Pac. R. Co. v. Moffitt, 75 R. Co. v. Moffitt, 75 Ill. 524; Wa- Ill. 524; Columbus, Chicago & I. C. bash, St. Louis & Pac. Ry. Co. v. Ry. Co. v. Skidmore, 69 Ill. 566; "For the purposes of answering for the liabilities of the constituent corporations," said the Indiana court, "the consolidated company should be deemed to be merely the same as each of its constituents, their existence continued in it, under the new form and name, their liabilities still existing as before, and capable of enforcement against the new company in the

Co. v. Jones, 29 Ind. 465, 95 Am. Dec. 654; Columbus, Chicago & I. C. Ry. Co. v. Powell, 40 Ind. 37; Jeffersonville, Madison & I. R. Co. v. Hendricks, 41 Ind. 48; Eaton & Hamilton R. Co. v. Hunt, 20 Ind. 457; Louisville, New Albany & C. Ry. Co. v. Boney, 117 Ind. 501; Berry v. Kansas City, Ft. Scott & M. R. Co., 52 Kan. 759, 39 Am. St. Rep. 371, 52 Kan. 774, 39 Am. St. Rep. 381; Mississippi Valley R. Co. v. Chicago, St. Louis & N. O. R. Co., 58 Miss. 846; Thompson v. Abbott, 61 Mo. 176; Boardman v. Lake v. McAlpine, 129 U. S. 305. Shore & Michigan Southern Ry. Co., 84 N. Y. 157; Miller v. Lancaster, 5 Cold. (Tenn.) 514; Houston & Texas Central R. Co. v. Shirley, 54 Tex. 125; Indianola R. Co. v. Fryer, 56 Tex. 609; Langhorne v. Richmond Ry. Co., 91 Va. 369; Tompkins v. Augusta Southern R. Co., 102 Ga. 436; United Ind. App. 533.

ganization, see ante, § 342.

to the consolidation of corporations of different states, see, in ad-

post, § 362(e), note 472.

A consolidated railroad company is liable on a contract by one of the consolidating companies that, in consideration of a grant of a right of way to it, it would so construct its road as to protect the grantor's lands from overflow. T. R. Co., 37 Ark. 23.

wards consolidated with another the consolidating

Indianapolis, Cincinnati & L. R. company under an agreement by which the consolidated company takes the property subject to the consolidating company's debts, the judgment is binding on the consolidated company. Chicago & Southeastern Ry. Co. v. Galey, 141 Ind. 360.

> The consolidated corporation takes the property of a consolidating corporation subject to an executory contract of sale made by it before the consolidation. McAlpine v. Union Pacific Ry. Co., 23 Fed. 168; Union Pacific Ry. Co.

When an action is brought to recover from a consolidated corporation on a cause of action which originally accrued against one of the constituent corporations, the declaration or complaint show against which company it accrued, and aver such facts as will subject the new company to States Capsule Co. v. Isaacs, 23 liability upon it. It is improper to charge the transaction as having As to the rule in case of reor- been by or with the consolidated unization, see ante, § 342. company. Marquette, Houghton As to the application of this rule & Ontonagon R. Co. v. Langton, 32 Mich. 251. And see Indianapolis, Cincinnati & L. R. Co. v. Jones, 29 dition to the cases above cited, Ind. 465, 95 Am. Dec. 654; Langhorne v. Richmond City Ry. Co., 91 Va. 369.

Where a corporation, after it issued bonds and secured had them by a mortgage, was consolidated with two other corporations under a statute which vested the property of the three original cor-Sappington v. Little Rock, M. R. & porations in the consolidated cor-R. Co., 37 Ark. 23.

poration, and provided that the When a railroad company confirst corporation was not to be demns land for a right of way, and relieved from any liability, and a judgment for damages is ren-that, after the consolidation, all dered against it, and it is after the franchises and property of corporations same way as if no change had occurred in its organization or name." 404

—(2) Statutory liabilities.—As is stated above, the statutes authorizing consolidation often expressly provide that the consolidated corporation shall be liable for the debts and other liabilities of the consolidating corporations. The extent of the liability under the statute depends, of course, upon its terms. 405

should belong to the consolidated members of the old companies. corporation, it was held that the consolidated corporation, having become the owner of the property of the first, might purchase its outstanding bonds, and either hold them as any other creditor, or pay, and extinguish them for the relief of the mortgaged property. Shaw v. Norfolk County R. Co., 16 Gray (Mass.) 407.

On consolidation of railroad companies, the new company was held bound to recognize mileage books issued by the old. Tompkins v. Augusta Southern R. Co., 102 Ga. 436.

Where a statute authorized the consolidation of two railroad companies "upon such terms as may be agreed upon," and did not declare how the existing liabilities or obligations of either should be settled or performed, and a consolida-tion was effected thereunder by a written contract providing for the absorption of one of them by the other, but making no provision at all for a certain class of liabilities existing against the absorbed company, it was held that these liabilities became binding upon the new company, at least to the extent of the assets of the absorbed company, or of its ability to perform the contracts out of which such liabilities arose. Tompkins v. Augusta Southern R. Co., 102 Ga. 436.

consolidated corporation takes the property and assumes the liabilities of the old corporations in the exact condition in which they exist at the time of the conFranklin Life Ins. Co. v. Adams, 90 Ill. App. 658.

404 Indianapolis, Cincinnati & L. R. Co. v. Jones, 29 Ind. 465, 95 Am. Dec. 654.

"The rule which the authorities support seems to be, that where one corporation goes entirely out of existence by being incorporated into another, if no arrangements are made respecting the property and liabilities of the corporation that ceases to exist the corporation into which it is merged will succeed to all its property, and be answerable for all its liabilities." Louisville, New Albany & C. Ry. Co. v. Boney, 117 Ind. 501.

405 See the New York Business Corporations Law, ante, § 349(b). In New York, under a statute authorizing consolidation of railroad companies, and making the consolidated company liable for the debts of the consolidating companies, "except mortgages," it was held that the consolidated company was liable on bonds which had been issued by a consolidating company, although it had given a mortgage to secure the same, as the exception of mortgages did not except debts secured by mortgage, so as to prevent the creditor from collecting the bonds from the consolidating corporation without resorting to the mortgage security. The statute, it was held, simply confined the lien created by the mortgage to the property owned prior to the consolidation by the comsolidation, except as to suits then pany giving it. Polhemus v. pending, and such liability cannot Fitchburg R. Co., 123 N. Y. 502, afterwards be extended by acts of affirming 50 Hun, 397; Janes v.

No provision in the agreement between corporations to consolidate can affect the right of creditors, not parties to the agreement, to recover on their claims against the new corporation, as provided by the statute. 406 But it is otherwise where the creditors are parties to the agreement. An agreement for consolidation which provides that the new corporation shall owe no debts on account of the business of the constituent companies prevents recovering from the new corporation, by stockholders of the constituent companies who have signed it, upon any claims which they may have had against the constituent companies.407

A statute imposing liability upon a consolidated company for debts of the consolidating companies is not retrospective, and does not apply to consolidations effected before its passage. As to these, the question of liability must be determined irrespective of the statute.408

(3) Contract to exchange stock for bonds.—In a Massachusetts case, a railroad company, having leased its road, issued bonds guarantied by the lessee, and which provided that the holders might convert them into shares of its (the lessor's) stock at par at any time after the completion of its road. After the road was completed, the two corporations were con-

railroad companies and providing that all debts and liabilities incurporation, and

Wall. (U. S.) 604.
The New York statute (Laws The New York statute (Laws 1892, c.340) authorizing street railing Co., 154 N. Y. 268. road companies to consolidate, the consolidated company to succeed to ing Co., 154 N. Y. 268. the rights of the consolidating corporations, and to assume their burbash & W. R. Co., 62 Ill. 477.

Fitchburg Ry. Co., 50 Hun (N. Y.) dens, obligations, and liabilities imposed by law, is not objectionable Under a statute consolidating because it does not require the consent of the abutting owners and the local authorities, as required red by either should attach to the by law, since the assumption of new corporation, it was held that the burdens, obligations, and liaa liability of one of the old cor- bilities imposed by law of the conporations to pay an internal rev- solidating companies necessarily inenue tax on scrip dividends declar- cludes all obligations to which ed by it attached to the new cor- such companies were subject, inwas enforceable cluding the obligation to obtain against it and its property. Bailey such consent when required by law. v. New York Central R. Co., 22 Bohmer v. Haffen, 161 N. Y. 390, affirming 35 App. Div. 381.

solidated under a statute which provided that the corporation so established should be subject to "all the duties, restrictions, obligations, debts, and liabilities to which, at the time of the union," either of said corporations might be subject, and that "all claims and contracts against either corporation" might be enforced by suit or action, to be commenced and prosecuted against the new corporation. After the consolidation, a holder of such bonds made a demand upon the new corporation for shares of stock as provided therein, but offered to accept in satisfaction of his demand shares of stock in the new corporation, and the demand was refused. It was held that the new corporation was bound by the provision in the bonds, and that the bondholder could maintain an action against it to recover the damages occasioned to him by its refusal of his demand.409

In a later case, it appearing that the corporations were consolidated on the footing of perfect equality between the shares of their stock and the shares of stock in the new corporation, it was held that the new corporation was bound to deliver its own shares in exchange for the bonds, or to pay the damages occasioned by its refusal to do so.410

(c) Liability for torts of consolidating corporations.—In conferring authority to consolidate, the legislature may exempt the consolidated corporation from any liability for the torts

409 John Hancock Mutual Life Ins. Co. v. Worcester, Nashua & Rochester R. Co., 149 Mass. 214.

410 Day v. Worcester, Nashua & Rochester R. Co., 151 Mass. 302.

For other cases involving the rights of holders of bonds convertible into stock, see Rosenkrans v. Lafayette, Bloomington & M. R. Co., 18 Fed. 513; Tagart v. Northern Central Ry. Co., 29 Md. 557; Child v. New York & New England R. Co., 129 Mass. 170; India Mutual Ins. Co. v. Worcester, Nashua & Rochester R. Co. (Mass.) 25 N. E. 975. And see post, West End Street Ry. Co., 173 Mass. § 422.

The Massachusetts statute of 1879 (chapter 151), "authorizing" an increase in the capital stock of a street railway company, and appropriating a portion of such stock to the payment or redemption of certain bonds of the company, which the holders thereof should be entitled to convert into stock at maturity, does not entitle a holder of such bonds to stock in the successor of such corporation, with which it was consolidated before the stock authorized by the statute was issued, and before maturity of the bonds. Parkinson v.

of the consolidating corporations, or it may expressly impose such liability. If it expressly declares that the consolidated corporation shall be subject to all the liabilities of the consolidating corporations, it thereby imposes liability for the negligence and other torts of the consolidating corporations, as well as on contracts. And in the absence of any provision at all, one way or the other, the consolidated corporation impliedly assumes such liability, as it is to be presumed that such was the intention.<sup>411</sup>

Of course the consolidated corporation may expressly assume such liability, as well as liability on contracts. Where a consolidated railroad company assumes the payment of all debts and liabilities, and the fulfillment of all obligations, of the consolidating companies, it becomes liable to an action to recover damages for personal injuries caused by the negligence of one of the consolidating companies prior to the consolidation.<sup>412</sup>

The effect of continuance of the consolidating corporations for the purpose of adjusting their liabilities, and the effect of

411 Berry v. Kansas City, Ft. Scott & M. R. Co., 52 Kan. 759, 39 Am. St. Rep. 371, 52 Kan. 774, 39 Am. St. Rep. 381; Langhorne v. Richmond R. Co., 91 Va. 369; St. Louis & San Francisco R Co. v. Marker, 41 Ark. 542; Chicago, Rock Island & Pac. R. Co. v. Moffitt, 75 Ill. 524; Indianapolis, Cincinnati & L. R. Co. v. Jones, 29 Ind. 465, 95 Am. Dec. 654; Louisville, New Albany & C. Ry. Co. v. Boney, 117 Ind. 501; Louisville, E. & St. L. Consolidated R. Co. v. Summers, 131 Ind. 241; Texas & Pacific Ry. Co. v. Murphy, 46 Tex. 356; Warren v. Mobile & Montgomery R. Co., 49 Ala. 582.

Compare, however, Cotzhausen v. H. W. Johns Mfg. Co. of New Jersey, 100 Wis. 473.

In an Indiana case, a consolidated railroad company was held liable for stock killed by one of the

corporations constituent the consolidation, although there was no provision to this effect in the statute or in the agreement of the corporations under which the consolidation was effected. The court said in this case: "For the purposes of answering for the liabilities of the constituent corporations, the consolidated company should be deemed to be merely the same as each of its constituents, their existence continued in it, under the new form and name, their liabilities still existing as before, and capable of enforcement against the new company in the same way as if no change had occurred in its organization or name." Indianapolis, Cincinnati & L. R. Co. v. Jones, 29 Ind. 465, 95 Am. Dec.

<sup>412</sup> St. Louis & San Francisco R. Co. v. Marker, 41 Ark. 542. actions and judgments against them upon the remedy against the consolidated company, are elsewhere considered. 413

- (d) Consolidation after foreclosure sale.—The rule that a consolidated corporation is liable for the debts of the constituent corporations rests upon agreement, express or implied, and applies only to voluntary consolidations. It does not apply where the property and franchises of a corporation are sold, under a decree foreclosing a mortgage thereon, to another corporation, and the property and franchises of both are then consolidated in the hands of the purchasing corporation. In such a case, the consolidated corporation is not liable, unless made so by valid statutory provision, for the debts of the corporation whose property and franchises have been sold.<sup>414</sup>
- (e) Continuance of consolidating corporations.—Statutes authorizing consolidation or articles of consolidation sometimes provide for continuance of the existence of the constituent corporations for the purpose of adjusting their liabilities, and questions have arisen as to the effect of this upon the liability of the consolidated corporation.

It has been held that, where a statute authorizing the consolidation of corporations, or articles of consolidation, provide that the consolidated corporation shall not be liable for the debts of the consolidating corporations, which shall continue in existence for the purpose of adjusting all claims and demands against them, and that the consolidation shall not prevent the enforcement of any valid obligation or liability of any constituent corporation against the property transferred by it, a creditor of one of the constituent corporations cannot maintain an action against the consolidated corporation until he has brought an action against the constituent corporation, and reduced his claim to judgment.<sup>415</sup>

In an Alabama case, however, where an act consolidating

 $_{\rm 413}\,\rm See$  infra, this section, (e). ante, § 342(c), and cases there cited.

<sup>414</sup> Houston & Texas Central R. 415 Whipple v. Union Pacific Ry. Co. v. Shirley, 54 Tex. 125. See Co., 28 Kan. 474.

two railroad companies into one under a new name provided that the consolidation and change of name "should in no way affect the rights of the creditors of said companies, and their separate existence should be continued as to all the rights and remedies of creditors," that the president of the new company "should be held in law, as to service of process, as the president of" each of the old companies, and that the new company might "dispose of any property, real or personal, held by each of said companies, and make and execute titles for the same, and sue for and recover in its name all debts, dues, and demands, of every kind and description whatsoever. due to each of said companies," it was held that an action at law might be maintained against the new company to recover damages for personal injuries caused by the wrongful act of one of the old companies. "The purpose of the act," said the court in this case, "in preserving the separate existence of the companies, was not to prescribe the manner in which demands against them were to be enforced, but, out of abundant caution, to make sure that no remedy for their enforcement should be lost or impaired by the amalgamation. If a case should arise in which the new organization would not be amenable for the liability of the others, this provision saved the remedv."416

- (f) Taking renewal notes.—When corporations are consolidated into a new corporation under a statute or agreement making the new corporation liable for all the debts and on all the contracts of the old corporations, outstanding notes of the old corporations are not paid or discharged, so as to relieve the new corporation of liability thereon, by the taking of renewal notes after the consolidation, unless the parties so intend.<sup>417</sup>
- (g) Taking judgment against old corporation.—Where the statutes in relation to consolidation make the consolidated corporation liable for all debts or liabilities of the consolidating corporations "existing or accrued prior to such consolidating corporations".

<sup>416</sup> Warren v. Mobile & Montgomery R. Co., 49 Ala. 582.

417 In re Utica National Brewing Co., 154 N. Y. 268.

tion," and declare that "actions may be brought and maintained, and recovery had therefor, against such consolidated company," it might be argued that, in the absence of any further provision, the consolidated company is not liable on a judgment rendered against one of the constituent companies after the consolidation upon a cause of action accruing, and in an action pending, before the consolidation, on the ground that the cause of action or liability merges in the judgment, which is a new debt accruing after the consolidation.418

However this may be, it has been held that the consolidated corporation is liable on such a judgment, where the statute under which the consolidation is effected expressly declares that it shall not affect suits pending, nor causes of action, etc., against the constituent corporations.419

(h) Remedy against consolidated corporation—(1) Action at law.—A person having a right to enforce against a consolidated corporation a liability originally incurred by one of the consolidating corporations, whether arising from contract or tort, need not proceed in equity, but may maintain an action at law.

"There has been some question whether the consolidated company could be sued in an action at law for the liabilities of the companies composing it, or whether the proceeding must be in equity. But the better view seems to be that when a consolidation has been authorized and made, it confers all the rights, property, and franchises of the old company upon the new or consolidated company, and subjects it to all the liabilities of the old companies; and an action at law may be brought against the new or consolidated company for the debts or torts of the old companies. The question is not whether the consolidation compels a creditor to accept the defendant corporation as a new debtor against his will, or a person who has been

<sup>418</sup> See Chicago, Santa Fe & C. Re Utica National Brewing Co., Ry. Co. v. Ashling, 160 Ill. 373. 154 N. Y. 268. The contrary, however, was held under the New York statute, in Co. v. Ashling, 160 Ill. 373.

injured to resort to a stranger for satisfaction, but whether it empowers the creditor or the person injured to resort, if he desires to do so, in the first instance, to the corporation which by the terms of the consolidation is made liable to him. privity, some cases say, necessary to support this action, is created by the statute authorizing the consolidation and the purchase and conveyance under it. Other authorities place the right to bring such action on the ground that the effect of the consolidation is, as to the liabilities of the old company. not to dissolve the corporation which is the immediate debtor, but to continue its existence in the consolidated corporation. If, by authority of law and the act of the parties, the consolidated corporations are molded into one with none of their rights impaired, and none of their responsibilities lessened, there is no good reason why the same proceedings may not be had against the new corporation as might have been had against the old to compel payment of liabilities. It avoids circuity of action. It allows the party with whom the contract was made, or to whom the injury was done, to proceed directly against the corporation which, by virtue of the consolidation proceedings, is made liable for it."420

---(2) Equity jurisdiction.—A creditor of a consolidating corporation may certainly proceed in equity to enforce his rights against the consolidated corporation, or against the property of the consolidating corporation in its hands, if it has no adequate remedy at law.421 It has been held, however, that where, by the statute under which the consolidation is effected, or otherwise, the consolidated corporation is liable for the debts of the consolidating corporations, the creditor's remedy at law is complete and adequate, and he cannot proceed against the consolidated corporation in equity. 422

<sup>420</sup> Langhorne v. Richmond Ry. Jones, 29 Ind. 465. 95 Am. Dec. Co., 91 Va. 369; Western Union 654; and cases in note 422, infra. R. Co. v. Smith, 75 Ill. 496; Sapand See many other cases cited pington v. Little Rock, M. R. & in notes 403 and 411, supra. T. R. Co., 37 Ark. 23; Indianapolis, Cincinnati & L. R. Co. v. 421 Harrison v. Arkansas Valley

# Rights of creditors against consolidating corporations and their property-Where consolidating corporations are dissolved.

If a consolidation is effected by the creation of an entirely new corporation, and dissolution of the consolidating corporations, creditors of the consolidating corporations cannot maintain an action against them after the dissolution, unless their existence is continued for the purpose of adjusting their liabilities, and of suits by or against them, for the creditors of a corporation cannot prevent consolidation or dissolution, and a corporation cannot be sued after its dissolution. 423 The only remedy of their creditors is either against the consolidated corporation, or, in equity, against the assets of the consolidating corporations in its hands.

That the creditors of the consolidating corporations may follow their assets into the hands of the consolidated corporation in such a case can admit of no question; and they cannot be deprived of this right by the consolidation agreement or by the statute authorizing the consolidation, unless the authority to consolidate was given before they became creditors. 424 thority to consolidate was conferred when the contract was entered into, the creditor must be assumed to have contracted with reference to the existence of the power, and he may be restricted to a remedy against the consolidated corporation. 425

Waiver-Laches-Bona fide purchasers.-A creditor of a con-

Ry. Co., 4 McCrary, 264, 13 Fed. 522; post, § 357.

422 Arbuckle v. Illinois Midland Ry. Co., 81 Ill. 429; United New Jersey Railroad & Canal Co. v. Hoppock, 28 N. J. Eq. 261.

423 Ante, §§ 303, 329; post, § 361; People v. Empire Mutual Life Ins. Co., 92 N. Y. 105; Houston & Texas Central R. Co. v. Shirley, 54 Tex. 125; Indianola R. Co. v. Fryer, 56 Tex. 609; In re Manchester & London Life Assurance & Loan Ass'n, L. R. 9 Eq. 643.

424 Ante, § 349(g); Chicago, Rock Island & Pac. R. Co. v. Moffitt, 75 Ill. 524; New Bedford R. Co. v. Old Colony R. Co., 120 Mass. 397; Market Street Ry. Co. v. Hillman, 109 Cal. 571.

In case of consolidation, the liabilities of the consolidating companies cannot be transferred to the consolidated company without the consent of the creditors. Market Street Ry. Co. v. Hillman, 109 Cal. 571.

425 Indianola R. Co. v. Fryer, 56 Tex. 609.

solidating corporation may waive his right to follow its assets into the hands of the consolidated corporation, or he may lose the right by laches in asserting it, or by the intervention of rights of bona fide purchasers or incumbrancers for value. If a creditor of one of the consolidating corporations sues and recovers a judgment against the consolidated corporation on his claim, he cannot afterwards enforce his judgment against property of the consolidating corporation conveyed to bona fide purchasers before recovery of the judgment. 426

Where consolidating corporation is not dissolved.-Where a consolidating corporation is not dissolved by the consolidation, as in the case of consolidation by merger of one corporation in another, which continues in existence, 427 or where the existence of consolidating corporations is continued for the purpose of adjusting their liabilities, creditors of the undissolved consolidating corporation may sue it and recover judgment on their claims notwithstanding the consolidation, and may then enforce the judgment against its property in the hands of the consolidating corporation, 428 unless he has waived his rights in this respect, or lost the same by laches, or by the passing of the property into the hands of bona fide purchasers.429

Bankruptcy or insolvency proceedings.—If a consolidating corporation is not dissolved by the consolidation, bankruptcy or insolvency proceedings may be instituted against it by its creditors, as if no consolidation had been effected. 430

#### § 358. Effect of consolidation as to liens.

The consolidation of corporations has no effect whatever upon liens, by mortgage or otherwise, upon the property of the consolidating corporations, but the consolidated corpora-

<sup>428</sup> McMahan v. Morrison, 16 Conn. 544; Chicago, Santa Fe & Ind. 172, 79 Am. Dec. 418. C. Ry. Co. v. Ashling, 160 Ill. 373.

<sup>427</sup> Ante, § 354.
428 In re Utica National Brew- Ind. 172, 79 Am. Dec. 418. ing Co., 154 N. Y. 268; Platt v. 430 Platt v. New Y New York & Boston R. Co., 26 R. Co., 26 Conn. 544.

<sup>430</sup> Platt v. New York & Boston

tion takes the property subject thereto. A maritime lien is not affected by consolidation. As a

A consolidated corporation takes the property of the consolidating corporations subject to unrecorded mortgages executed by the consolidating corporations prior to the consolidation, and it cannot defeat such a mortgage by alleging ignorance thereof.<sup>433</sup> The lien of such a mortgage has precedence of the liens of a judgment creditor of the consolidated corporation, and is good as against a purchaser under execution on such a judgment.<sup>434</sup>

The lien of a mortgage given by one of the consolidating corporations will cover, in the hands of the consolidated corporation, not only the specific property which it covered in the hands of the old corporation, but also all acquisitions which issue from and become a part of the estate.<sup>435</sup>

Where one of the consolidating corporations has notice of a lien upon its property, the consolidated corporation is chargeable with such notice.<sup>436</sup>

Though the consolidated corporation assumes the contract liabilities of the consolidating corporations, the unsecured creditors of the consolidating corporations have no specific lien on their property in the hands of the consolidated corpora-

481 The Key City, 14 Wall. (U. S.) 654; Central Railroad & Banking Co. v. Georgia, 92 U. S. 665, 1 Keener's Cas. 96; Eaton & Hamilton R. Co. v. Hunt, 20 Ind. 457; Mississippi Valley R. Co. v. Chicago, St. Louis & N. O. R. Co., 58 Miss. 846; Hamlin v. Jerrard, 72 Me. 62; Schutte v. Florida Central R. Co., 3 Woods, 692, Fed. Cas. No. 17,434; Rutten v. Union Pacific Ry. Co., 17 Fed. 480.

If a creditor of a corporation has a specific lien upon the income of its property, he may enforce the same in equity against a corporation formed by its consolidation with another, and which has acquired the property. Rutten v. Union Pacific Ry. Co., 17 Fed. 480.

As to a mechanic's lien, see United Mines Co. v. Hatcher (C. C. A.) 79 Fed. 517.

 $^{432}$  The Key City, 14 Wall. (U. S.) 654.

483 Mississippi Valley R. Co. v. Chicago, St. Louis & N. O. R. Co., 58 Miss. 846.

434 Mississippi Valley R. Co. v. Chicago, St. Louis & N. O. R. Co., 58 Miss. 846.

435 Hamlin v. Jerrard, 72 Me. 62; Central Railroad & Banking Co. v. Georgia, 92 U. S. 665, 1 Keener's Cas. 96.

As to the rights under a railroad mortgage, see these cases.

<sup>436</sup> Schutte v. Florida Central R. Co., 3 Woods, 692, Fed. Cas. No. 17,434.

tion.437 And it follows that ordinarily they have no priority over bona fide mortgagees of the consolidated corporation. 438 The consolidation agreement or statute, however, may be such as to give unsecured creditors of the consolidating corporations a lien on their property in the hands of the consolidated cor-Thus, where a railroad consolidation agreement stipulated that certain equipment bonds of a consolidating company should be protected by the consolidated company, it was held that the holders thereof acquired the right to require that the property of the company issuing them be applied to their payment, and that, as the consolidation agreement was a matter of public record, they could enforce this right against any person deriving title to such property from the consolidated company.439

## § 359. Rights and liabilities of stockholders—Rights in general.

The right of stockholders to object to a consolidation, and the various rights and remedies of dissenting stockholders, are elsewhere considered. 440 This section relates to the rights and liabilities of stockholders after a valid consolidation to which they assent.

When corporations are consolidated under legislative authority, the rights of the stockholders depend upon the statute under which the consolidation is effected, and the agreement to consolidate, in so far as it is not in violation of the statute. The statute or the agreement, or both, generally provide that the consolidated corporation shall issue shares of its stock to the stockholders of the consolidating corporations, and shall pay a certain sum in cash to those of the stockholders who shall elect to take such payment instead of stock.441

<sup>487</sup> Wabash, St. Louis & Pac. 440 Ante, § 349(f).
Ry. Co. v. Ham, 114 U. S. 587. 441 See the New York statute,
438 Wabash, St. Louis & Pac. ante, § 349(b). And see, for the
Ry. Co. v. Ham, 114 U. S. 587. construction of such a statute or is & Pac. Ry. Co., 45 Ohio St. 1 Bosw. (N. Y.) 1. 592.

<sup>439</sup> Compton v. Wabash, St. Lou- agreement, Butterfield v. Spencer, Where, after a subscriber for

Stockholders of the consolidating corporations may maintain an action directly against the consolidated corporation to compel the issue of stock to them in accordance with the agreement of consolidation, or to recover damages for its failure or refusal to do so.442

The statute under which a consolidation is effected, or the articles or agreement of consolidation, may be such as to constitute the stockholders of the consolidating corporations stockholders of the consolidated corporation, without any further action on their part or on the part of the consolidated corporation.448

When an agreement of consolidation is entered into between the stockholders of corporations, as provided by a statute authorizing consolidation, and providing for such an agreement, it is only the terms of this agreement that are binding upon the consolidated company. It is not bound by any secret agree-

stock in a corporation has paid ness to a new corporation, under ten per cent. thereon, the corpo- an agreement by which the new ration is consolidated with an company is to issue its stock to other under an agreement by the stockholders of the old comaccount of his subscription, where more than the ten per cent., or that he was entitled to full-paid stock in the original corporation. Babcock v. Schuylkill & Lehigh Valley R. Co., 133 N. Y. 420, af-firming 60 Hun, 583.

As to the rights of holders of bonds of the consolidating corporations convertible into stock, see ante, § 356(b)(3).

442 Fee v. New Orleans Gas Light Co., 35 La. Ann. 413; Anthony v. American Glucose Co., 66 Hun (N. Y.) 634, 146 N. Y. 407. See ante, § 345(f).

Where several corporations, for purpose of consolidating, transfer their property and busi- ing Co., 33 Mich. 2.

which the stockholders are to re-panies in exchange for their stock ceive consolidated stock in place in the latter, a stockholder may of their original stock, a stock- maintain an action against the holder cannot compel the consolinew corporation to compel it to dated corporation to issue to him issue its stock to him, in accordfull-paid certificates of stock, on ance with the agreement; and the fact that the new corporation has there is no proof that he has paid issued to the old corporation the amount of the new stock due to its shareholders is no defense, if the plaintiff did not consent. Anthony v. American Glucose Co., 66 Hun (N. Y.) 634, 146 N. Y. 407.

Nor is it any defense to show that the plaintiff has refused to pay his share of the debts of his old company, if there is no proof that payment thereof was made a condition precedent to his right to stock in the new corporation, or that he has been assessed for such payment, or that there is a lien for such payment on the new stock.

448 See Copeland v. Minong Min-

ment between the stockholders of the consolidating companies. 444

Estoppel.—When corporations are consolidated under legislative authority, and all the property and rights of the consolidating corporations are transferred by the agreement of consolidation, or by the statute authorizing or effecting the consolidation, to the consolidated corporation, a stockholder of one of the consolidating corporations, who surrenders his stock and accepts stock in the new corporation, cannot afterwards complain of the transfer, "for it will not do for him to avail himself of the advantages of the change, without at the same time submitting to any inconvenience or loss which may attend the substitution of the one for the other." 445

Liabilities of stockholders.—Stockholders who consent to a consolidation of their corporation with another are liable to the consolidated corporation on their subscriptions to the stock of the consolidating corporation, transferred to the former under the agreement of consolidation.<sup>446</sup>

When the consolidating corporations are dissolved, and an entirely new corporation is created, the statutory liability of stockholders for the debts of the consolidated corporation is determined by the law in force at the time of the consolidation. As we have seen, they cannot attack the validity of the consolidation, or of the statute under which it was effected, for the purpose of escaping such liability. 448

Fraud upon stockholders.—When corporations enter into an agreement to consolidate, and one of them, or its stockholders, perpetrates a fraud upon the stockholders of the other, the latter are entitled to relief. The issue of a scrip dividend by a corporation in fraud of another corporation, with which it

<sup>444</sup> Trenton Passenger Ry. Co. v. Wilson, 55 N. J. Eq. 273.

<sup>445</sup> Union Canal Co. v. Young, 1 Whart. (Pa.) 410, 30 Am. Dec. 212. 446 Ante, § 355(c).

<sup>447</sup> Tibballs v. Libby, 87 III. 142; Gardner v. Minneapolis & St. Louis Ry. Co., 73 Minn. 517.

<sup>448</sup> Gardner v. Minneapolis & St. Louis Ry. Co., 73 Minn. 517; ante, § 353.

is about to consolidate, is voidable as against the stockholders of the other corporation.449

## § 360. Authority of officers.

The officers of the consolidated corporation are the successors of the officers of one of the consolidating corporations, in so far as the management of the property derived from it is concerned, and therefore they are bound by proceedings commenced against the latter.450

### Effect of consolidation on actions or proceedings.

In a Mississippi case it was held that a suit against a corporation did not abate, and might be prosecuted to judgment, after the corporation was consolidated with another, notwithstanding the consolidation was authorized by the legislature, and, apparently, notwithstanding the fact that there was no statute declaring that pending actions should not abate. court said that the action of the legislature authorizing the consolidation, and the action of the corporation under such authorization, could not defeat or prejudice the right of the plaintiff in suits pending against it.451

This decision, however, cannot be sustained in any case where the consolidating corporations are dissolved. corporation is dissolved, it ceases to exist for any purpose, and

without the knowledge of the othcapital stock, with interest, payable at the option of the company, thus increasing their indebtedness to that amount, certificates of indebtedness being issued in accordance with the resolution; and consolidation was aft- Central R. Co., 52 Miss. 159.

449 Bailey v. Citizens' Gas Light erwards effected between the com-Co., 27 N. J. Eq. 196. In this case, panies, without any knowledge on while negotiations were pending the part of the other company as between two gas companies for to such resolution and increase of their consolidation upon a certain indebtedness. Upon a bill filed basis of indebtedness, one of the for the purpose, it was held that companies passed a resolution, the scrip would be declared void, and the company issuing it reer, declaring a scrip dividend of strained from recognizing it as a ten per cent. on the amount of its valid obligation, or permitting its transfer.

> 450 Prouty v. Lake Shore & Michigan Southern Ry. Co., 52 N. Y. 363.

> 451 Shackleford v. Mississippi

the overwhelming weight of authority is to the effect that no action can be commenced by or against it after the dissolution. and pending actions abate, unless there is some statutory provision to the contrary. 452 And the legislature may dissolve a corporation without the consent of its creditors, although it cannot prevent them from following and subjecting its property in equity. 453 These principles necessarily apply where corporations are dissolved by a consolidation under legislative authority,454 so that no action can be brought against them, after the consolidation; and actions pending against them at the time of the consolidation abate,455 unless their existence is expressly continued by statute, as is sometimes the case. 456

Pending actions or proceedings by or against the consolidating corporations may be revived against the new corporation, or it may be substituted as defendant. 457 When a corporation

452 Ante. § 329.

453 Ante, § 303.

454 Ante, § 354.

455 Thornton v. Marginal Freight Ry. Co., 123 Mass. 32, 1 Cum. Cas. 462; Indianola R. Co. v. Fryer, 56 Tex. 609; Kansas, Oklahoma & T. Ry. Co. v. Smith, 40 Kan. 192; Council Grove, Osage City & O. R. Co. v. Lawrence, 3 Kan. App. 274; Wagner v. Atchison, Topeka & S. F. R. Co., 9 Kan. App. 661.

456 See Baltimore & Susquehanna R. Co. v. Musselman, 2 Grant's Cas. (Pa.) 348; East Tennessee & Georgia R. Co. v. Evans, 6 Heisk. (Tenn.) 607; Edison Electric Light Co. v. Westinghouse, 34 Fed. 232; Edison Electric Light Co. v. United States Electric Lighting Co. (C. C. A.) 52 Fed. 300; ante, § 354.

457 Kinion v. Kansas City, Ft. Scott & M. R. Co., 39 Mo. App.

It has been held that proceedings instituted by a railroad company to condemn land for its road, which commissioners have made their report and award of damages, from which the landowner has appealed, do not be- Co. v. Hooper, 76 Cal. 404.

come void ab initio, nor abate, by reason of the consolidation and merger of the company with an-other railroad company, forming a new company, as provided by statute; but the rights in the land acquired by the condemnation proceedings survive, and pass to the new company, and it may be substituted as appellee. Day v. New York, Susquehanna & W. R. Co., 58 N. J. Law, 677.

On consolidation of a plaintiff corporation, the consolidated corporation may be substituted as a party under a statutory provision that an action shall not abate by the transfer of any interest therein, if the cause of action survive or continue, and that, in case of any disability of a party, the court may allow the action to be continued by or against his representative or successor in interest; and that, in case of any other transfer of interest, the action may be continued in the name of the original party, or the court may allow the party to whom the transfer is made to be substituted in the action. California Central Ry. is consolidated with another, and thereby dissolved, while an action is pending against it, the action does not continue as against the new corporation merely by reason of its succession, and no judgment can be rendered against the new corporation unless it is made a party.458

## § 362. Consolidation of corporations of different states.

- (a) In general.—As was stated at the beginning of this subdivision, and as was pointed out at some length in another chapter, 459 corporations created by different states may be consolidated by the concurrent action of the legislatures of the several states.460 This is often desirable in order to put all the corporations under one management, and to give them the same powers. Thus, if the line of a railroad company created by one state connects with the line of a railroad company created by another state, it may be desirable to consolidate the two companies, and thus put both lines under one management. This may be done under concurrent legislation in each state, but not otherwise, for neither corporation can have any authority to consolidate except by virtue of a law of the state creating it. Such consolidation may be of two or more existing corporations, each created by the laws of a different state, or, where a corporation created by one state owns property in another state, the latter state may make it also a corporation of its own with respect to such property.
- (b) Status of such a corporation in general.—As has been pointed out in another chapter,461 the effect of a consolidation of corporations created by different states under concurrent legislation in the several states is not to create a single corporation in all the states, as in the case of a consolidation

v. Harbin, 40 Ga. 706.

<sup>459</sup> Ante, §§ 37(g), 117.

<sup>460</sup> This is not prevented by the the United States conferring upon notes. congress the power to regulate

<sup>458</sup> Selma, Rome & Dalton R. Co. commerce between the several states. Boardman v. Lake Shore & Michigan Southern Ry. Co., 84 N. Y. 157.

As to the mode of effecting conprovision of the constitution of solidation, see ante, § 350, and

<sup>461</sup> Ante, § 117.

of corporations created by the same state, but to create a separate corporation in each state. For the purpose of conducting operations there is, in a sense, a consolidated corporation, for all the corporations are under one management, and may have precisely the same powers, and may consist of the same stockholders; but in contemplation of the law, there is a distinct corporation in each state, owing its existence to the law of that state, and that state only. This is necessarily so by reason of the fact that the laws of a state cannot operate bevond its territorial limits, and therefore cannot create or aid in creating a corporation in another state.

In a leading Illinois case it was said with respect to such legislation in Illinois and in Missouri creating corporations to maintain a bridge over the Mississippi river between those states: "The legislatures of this state and of Missouri cannot act jointly, nor can any legislation of the last-named state have the least effect in creating a corporation in this state. Hence, the corporate existence of the appellants, considered as a corporation of this state, must spring from the legislation of this state, which, by its own vigor, performs the act. The states of Illinois and Missouri have no power to unite in passing any legislative act. It is impossible, in the very nature of their organizations, that they can do so. They cannot so fuse themselves into a single sovereignty, and as such create a body politic which shall be a corporation of the two states, without being a corporation of each state or of either state. The only possible status of a company acting under charters from two states is, that it is an association incorporated in and by each of the states, and when acting as a corporation in either of the states, it acts under the authority of the charter of the state in which it is then acting, and that only, the legislation of the other state having no operation beyond its territorial limits." 462

<sup>462</sup> Quincy Railroad Bridge Co. v. (U. S.) 286; Baltimore & Ohio R. Adams County, 88 Ill. 615, 1 Keen- Co. v. Harris, 12 Wall. (U. S.) 65, er's Cas. 105. See, also, Ohio & Mississippi R. Co. v. Wheeler, 1 Black. western Ry. Co. v. Whitton's

The fact that corporations thus created or consolidated by the concurrent legislation of several states have the same stockholders, the same name, the same powers, and the same management, and conduct operations as if there were a single corporation only, has led some of the judges into speaking of them as a single corporation; 463 but that they are distinct corporations in each state is too well settled to be longer questioned. is impossible," said the Michigan court, "to conceive of one joint act, performed simultaneously by two sovereign states, which shall bring a single corporation into being, except it be by compact or treaty. There may be separate consent given for the consolidation of corporations separately created; but when the two unite they severally bring to the new entity the powers and privileges already possessed, and the consolidated company simply exercises in each jurisdiction the powers the

Adm'r, 13 Wall. (U. S.) 270; Mul-Massachusetts R. Co., 44 Vt. 613; ler v. Dows, 94 U. S. 444, 1 Cum. Baltimore & Ohio R. Co. v. Pitts-Cas. 53; Clark v. Barnard, 108 U. burgh, Wheeling & K. R. Co.. 17 S. 436; Nashua & Lowell R. Corp. W. Va. 812, 867; Henen v. Baltiv. Boston & Lowell R. Corp., 136 U. S. 356; Farnum v. Blackstone U. S. 356; Farnum v. Blackstone
Canal Corp., 1 Sumn. 47, Fed. Cas.
No. 4,675; Kahl v. Memphis & tice Swayne in the supreme court
of the United States that he saw
no reason "why several states
58 Ga. 523; Racine & Mississippi
R. Co. v. Farmers' Loan & Trust
Co., 49 Ill. 331, 95 Am. Dec. 595;
Newport & Cincinnati Bridge Co.
v. Woolley, 78 Ky. 523; State v.
Northern Central Ry. Co., 18 Md.
193; Chicago & Northwestern Ry.
Co. v. Auditor General, 53 Mich.
79; In re St. Paul & Northern Pa-79; In re St. Paul & Northern Pacific Ry. Co., 36 Minn. 85; McGregor v. Erie Ry. Co., 35 N. J. Law, 115; Easton Delaware Bridge Co. v. Metz, 32 N. J. Law, 199; Covington Bridge Company, the Sage v. Lake Shore & Michigan court said that the company was Southern Ry. Co., 70 N. Y. 220; "a single corporation clothed with & Pittsburgh R. Co., 51 Pa. St. 228; Sprague v. Hartford, Providence & F. R. Co., 5 R. I. 233; are identical, except as Mobile & Ohio R. Co. v. Barnhill, 91 Tenn. 395, 30 Am. St. Rep. 889; Richardson v. Vermont & v. Mayer, 31 Ohio St. 317.

burgh, Wheeling & K. R. Co.. 17 W. Va. 812, 867; Henen v. Balti-more & Ohio R. Co., 17 W. Va.

note 462, supra.

County of Allegheny v. Cleveland the powers of two corporations." "It acts," it was said, "under two charters, which in all respects are identical, except as to the source from which they emanate." Covington & Cincinnati Bridge Co.

corporation there chartered has possessed, and succeeds there to its privileges. It may well happen, as indeed it often has, that the consolidated company will be a corporation possessing in one state very different rights, powers, privileges and immunities to those possessed in another, and subject to very different liabilities. And after the consolidation each state legislates in respect to the road within its own limits, and which was constructed under its grant of corporate power, the same as it did before. it cannot follow the new organization with its legislation into When, therefore, two corporations another state. created in different states consolidate, though for most purposes they are not thereafter to be separately regarded, yet in each state the consolidated company is deemed to stand in the place of the corporation to which it there succeeded, and of its members, and consequently to be a citizen of that state for many purposes, while in the other state it would stand in the place of the other corporation in respect to citizenship there. ''464

- (c) Citizenship and residence.—In accordance with this view it has repeatedly been held that where corporations created by different states are consolidated by concurrent legislation in the several states, the consolidated corporation is to be considered as a citizen and resident of each state, for the purpose of suits in the federal courts, and for many other purposes. In each state it is there regarded as a domestic corporation.<sup>465</sup>
- (d) Whether "incorporated under the laws" of a particular state.—In a late New York case, in which a railroad corporation created by the laws of that state was consolidated with corporations created by the laws of several other states, under authority from the legislatures of all the states, the consolidated company taking the name of the New York company, it

<sup>464</sup> Per Chief Justice Cooley, in 465 Ante, § 117, and the cases Chicago & Northwestern Ry. Co. cited in note 462, supra. v. Auditor General, 53 Mich. 79.

was held that the consolidated corporation, since it owed its existence, not to the laws of New York alone, but to the concurrent legislation of the several states, was not "incorporated by and under a general and special law" of New York, within the meaning of the statute taxing stock corporations for the privilege of incorporation.466

This decision, however, seems to be opposed to the principle explained in the preceding paragraphs, and there are decisions in other jurisdictions to the contrary. As we have seen, when corporations created by or under the laws of different states are consolidated under legislation in each state, the consolidated company is, in contemplation of law, a corporation in and of each state. When acting as a corporation in any one of the states, it acts as a corporation of, and under authority of the charter from, that particular state, and that state only. has an existence as a domestic corporation in each state. would seem to follow necessarily from this, and so it has been held, that in each state the consolidated company is to be considered as "incorporated under the laws" of that state, within the meaning of a statute imposing a tax upon corporations. 467

(e) Conduct of business-Meetings, contracts, etc.-Though such a corporation is thus technically a distinct corporation in each state, and a resident of each state, and owes its existence and powers in each state to the laws of that state only, yet as it is under one management, consists of the same stockholders, and has the same powers in each state, it is in effect a consolidated corporation for the purpose of conducting its business and entering into contracts, etc.468

<sup>1</sup> Keener's Cas. 129.

<sup>467</sup> Quincy Railroad Bridge Co. v. County of Adams, 88 Ill. 615, 1 v. county of Adams, 88 in. 618, 1 45 Onio St. 504.

Keener's Cas. 105; Ohio & Mississippi R. Co. v. 'Weber, 96 Ill. 443. & Erie R. Co., 118 U. S. 161; Rand see Indianapolis & St. Louis cine & Mississippi R. Co. v. Farmer. Co. v. Vance, 96 U. S. 450; ers' Loan & Trust Co., 49 Ill. 331, Nashua & Lowell R. Corp. v. Bos- 95 Am. Dec. 595.

<sup>466</sup> People v. New York, Chicaton & Lowell R. Corp., 136 U. S. go & St. L. R. Co., 129 N. Y. 474, 356, 1 Keener's Cas. 118; and other cases cited in note 462, supra. See, also, Ashley v. Ryan, 49 Ohio St. 504.

Where corporations of different states are consolidated under concurrent legislation of the several states, with a capital stock which is a unit, and with only one set of shareholders, who have an interest, by virtue of their ownership of shares of the stock, in all its property everywhere, the consolidated corporation has a domicile in each state, and it or its shareholders can, in the absence of provision to the contrary, hold meetings and transact corporate business in any of the states, so as to bind the corporation as to its property everywhere. 469

Contracts made by the officers of the consolidated corporation, and mortgages executed by them upon its property in all the states, which purport to be made or executed by the consolidated corporation, will be regarded as made by the corporation of each state, and will be given the same effect as if the consolidated company were, in law as well as in reality, a single corporation.

It was said on this point in an Illinois case, in speaking of a mortgage given by railroad companies of Illinois and Wisconsin, consolidated under concurrent legislation in each state: "Where continuous lines of road, passing through different states, are consolidated by legislative authority. the consolidated company must, from the very nature of a corporation, be regarded as a distinct entity in each state, yet the objects of consolidation would be very liable to be defeated, unless the entire line should be placed under one board of di-The principle that a single corporation cannot be created by the joint legislation of two states, while an irresistible inference from the established law in regard to corporate bodies, is nevertheless a technical and abstract principle, and when adjoining states authorize consolidations, the consolidated lines are placed under a common board, with a

Co. v. People, 123 Ill. 467; Gui- Loan & Trust Co., 49 Ill. 331, 95 nault v. Louisville & Nashville Am. Dec. 595. R. Co., 41 La. Ann. 571; Coving-

<sup>469</sup> Graham v. Boston, Hartford ton & Cincinnati Bridge Co. v. & Erie R. Co., 118 U. S. 161. Mayer, 31 Ohio St. 319; Racine & See, also, Ohio & Mississippi Ry. Mississippi R. Co. v. Farmers'

common name and seal, such board will, naturally, act as if the consolidated lines made but one company, and when their contracts assume that form, the courts must, for the protection of the public, and to enforce good faith, hold, as we have done in this case, that the contract is to be construed as made by the corporation of each state in which the subject matter of the corporation lies; ut res magis valeat quam pereat."470

Where corporations of several states have been consolidated. and the consolidated company has executed a mortgage covering the property situated in the different states, the courts of either state have jurisdiction to foreclose the mortgage, not only as to the property situated within its limits, but also as to the property in the other states.471

And when a corporation formed by consolidation of corporations of different states assumes the obligations of the constituent corporations, it may be sued in either state upon a claim which arose originally against the constituent corporation created by the laws of the other state.472

(f) Control by courts and by legislatures.—Since a company formed by consolidation of corporations of different states has a corporate existence in each state the courts of either state have jurisdiction to control it, and may enjoin it from expending its funds for other than corporate purposes anywhere 473

In like manner, the legislature of each state has the same power to control and regulate the corporation, as a corporation of the state, as it had before the consolidation, except in so far as it may have surrendered such right by the grant of particular powers, privileges, or exemptions, in the statute authorizing the consolidation.474

Y. 157. And see the cases cited 470 Racine & Mississippi R. Co. v. Farmers' Loan & Trust Co., 49 ante, § 356.

<sup>478</sup> State v. Northern Central Ry. III. 331, 95 Am. Dec. 595. 471 Mead v. New York, Housa-Co., 18 Md. 193; Fisk v. Chicago, tonic & N. R. Co., 45 Conn. 199. Rock Island & Farb. (N. Y.) 513. Michigan Southern Ry. Co., 84 N. 474 Peik v. Chi Rock Island & Pac. R. Co., 53

<sup>474</sup> Peik v. Chicago & North-

### § 363. Remedies in case of unauthorized or defective consolida-

A stockholder may maintain a suit in equity to enjoin his corporation from entering into a consolidation, where there is no authority to consolidate, just as he may maintain such a suit to enjoin any other ultra vires act by the corporation, 475 provided he is not estopped by having assented or participated in the proceedings to consolidate.476 And he may maintain such a suit when the circumstances are such, as elsewhere explained, that the corporation has no right to consolidate without his consent, although there may be statutory authority for consolidation.477 A creditor, as we have seen, cannot, merely because he is a creditor, prevent a corporation from consolidating under legislative authority, and cannot maintain a suit to enjoin a consolidation.478

When corporations undertake to consolidate without any legislative authority, or where, in consolidating under legislative authority, there is such a failure to comply with the requirements of the law that there is not a corporation de jure, proceedings by the state through the attorney general may be instituted, as in other cases, to oust the consolidated company from the exercise of corporate powers.479

Under a statute prohibiting the consolidation of railroad companies having competing lines, and allowing any citizen to sue to enjoin its violation, it was held that a suit to restrain such 'a consolidation could be maintained by a private individual, without showing that he had any private interests, beyond those which every citizen is presumed to have, which would be damaged by the proposed consolidation.480

When corporations are authorized to consolidate, and at-

western Ry. Co., 94 U. S. 164; 42,72 Am. Dec. 685; Botts v. Simp-Maine Central R. Co. v. Maine, sonville & Buck Creek Turnpike 96 U.S. 499.

Road Co., 88 Ky. 54.

<sup>475</sup> Ante, § 210; post, § 539.

<sup>476</sup> Ante, § 353; post, § 553.

<sup>478</sup> Ante, § 349(g). 479 Ante, § 207.

<sup>477</sup> Post, chapter xxiv.; Lauman 480 Currier v. Concord R. Corp., v. Lebanon Valley R. Co., 30 Pa. St. 48 N. H. 321.

tempt to do so, colorably complying with the requirements of the law, and afterwards assume to act as a consolidated corporation, there is a de facto consolidated corporation, and its existence can only be questioned in a direct proceeding by the state. It has been held, therefore, that a bill to annul a consolidation of corporations, and to have declared void a mortgage executed by the consolidated company upon the aggregate property, on the ground that one of the consolidating companies had no legal corporate existence, cannot be maintained by stockholders of the consolidating corporations. Proceedings must be instituted, if at all, by the state through its attorney general.<sup>481</sup>

<sup>481</sup> Bell v. Pennsylvania, Slatington & N. E. R. Co. (N. J. Eq.) 10 Atl. 741. See ante, § 352.

### CHAPTER XIX.

### MEMBERSHIP IN CORPORATIONS IN GENERAL.

- I. ACQUISITION OF MEMBERSHIP.
  - § 364. In general.
    - 365. Necessity for a contract.
    - 366. Joint-stock corporations.
    - 367. Corporations not having a capital stock.
    - 368. Power to admit or exclude members.
- II. Loss of Membership.
  - § 369. In general.
    - 370. Transfer of shares or membership.
    - 371. Forfeiture of shares or membership.
    - 372. Surrender of shares, or withdrawal from membership.
    - 373. Disfranchisement or expulsion of members.
      - (a) In general.
      - (b) Grounds for disfranchisement or expulsion.
      - (c) Mode of procedure.
      - (d) Remedies for wrongful expulsion.
      - (e) Review by the courts.

### I. ACQUISITION OF MEMBERSHIP.

§ 364. In general.—To constitute one a member of a private corporation, there must be a contract between him and the corporation. No person, therefore, can be made or become a member of such a corporation without his consent and the consent of the corporation, express or implied.

Membership in a corporation having a capital stock divided into shares depends upon the ownership of shares by virtue of a valid contract with the corporation. Shares may be acquired—

- (1) By a subscription made before formation of the corporation, and accepted by the corporation when formed.
- (2) By a subscription both made and accepted after the corporation is formed.
  - (3) By purchase from the corporation after it is formed.

(4) By transfer from one person to another, either by agreement or by operation of law, to which the consent of the corporation is generally implied.

Membership in corporations not having a capital stock is acquired by virtue of a contract with the corporation, the nature and terms of which will vary according to the character of the corporation, and the provisions of its charter and by-laws, and which is generally evidenced by a certificate of membership, or other written instrument.

When a corporation is formed by the grant of a special charter, the original or charter members are generally named in the act, but no person can thus be made a member without his consent.

### § 365. Necessity for a contract.

It is within the power of the legislature to create a public corporation, like a city or town, and make the citizens members of the corporation without their consent.<sup>1</sup> But it is very different in the case of private corporations. In order that a person may be made or become a member of a private corporation, of whatever character, there must be a valid and completed contract between him and the corporation.<sup>2</sup>

No man can be made a member of a private corporation without his consent, express or implied.<sup>3</sup> Thus, as was shown in another chapter, a special act purporting to incorporate certain persons, naming them, can only have the effect of incorporating such of the persons named as consent or join in accepting the act.<sup>4</sup> And when the members of an existing corporation are,

<sup>1</sup> Ante, § 31.

<sup>&</sup>lt;sup>2</sup> Butler University v. Scoonover, 114 Ind. 381, 5 Am. St. Rep. 627, and other cases more specifically referred to in notes following.

<sup>3</sup> Ante, § 44; State v. Dawson, 16 Ind. 40, 1 Cum. Cas. 56, 1 Keener's Cas. 62, 1 Smith's Cas. 69; Yeaton v. Bank of Old Dominion, 21 Grat. (Va.) 593, 2 Smith's Cas. 808; Ellis v. Marshall, 2 Mass. 269, 3 Am. Dec. 49.

One who agrees to purchase a certain number of shares, or a proportionate part in case of oversubscription, from a syndicate to which they are to be issued, but who refuses, before issuance, to take them, and refuses to accept certificates, cannot be made a shareholder by a transfer to him on the books of the corporation. Greene v. Sigua Iron Co. (C. C. A.) 76 Fed. 947.

<sup>&</sup>lt;sup>4</sup> Ante, § 44; Ellis v. Marshall, 2 Mass. 269, 3 Am. Dec. 49.

by an act of the legislature, created into a new corporation, the act, assuming it to be valid as against such members as may dissent, does not make members of the old corporation members of the new, unless they consent, or in some way expressly or impliedly accept the act. Nor does it give the majority of the members of the old corporations the power to make others members of the new corporation without their consent. Such statutes generally, in express terms, require such consent or acceptance, but the necessity therefor is the same, whether it is expressly required or not.5

On the other hand, a person cannot acquire membership in a private corporation without the consent of the corporation, express or implied, given either by the stockholders or members collectively, as constituting or representing the corporation, or by its directors or other authorized officers or agents.<sup>6</sup> As we shall see more at length in a subsequent chapter, a mere subscription for shares in a corporation cannot constitute the subscriber a member of the corporation until it is either expressly cr impliedly accepted by the corporation, unless the corporation has offered its shares, so that the subscription is an acceptance of its offer.

#### § 366. Joint-stock corporations.

Most of the modern business corporations are stock corporations,—that is, corporations having a capital stock divided

Doc. 685; ante, § 44(a).

In Hamilton Mutual Ins. Co. v. held that an act of the legislature by which "the members of" sev- Mutual Ins. Co., 33 N. Y. 421. eral mutual fire insurance companies were made a new corporation, and which provided that it should not affect the legal rights of any person, and which was to take effect "when accepted by the members of said corporations,"

Filamilton Mutual Ins. Co. v. did not constitute a member of Hobart, 2 Gray (Mass.) 543; Gard- one of the old companies, who did ner v. Hamilton Mutual Ins. Co., not expressly assent to it, a mem-33 N. Y. 421; Lauman v. Lebanon ber of the new corporation, al-Valley R. Co., 30 Pa. St. 42, 72 Am. though the act was duly accepted by a majority of the members of each of the old companies. Hobart, 2 Gray (Mass.) 543, it was was a like decision under the same act in Gardner v. Hamilton

> American Live Stock Commission Co. v. Chicago Live Stock Exchange, 143 Ill. 210, 36 Am. St. Rep. 385; Starrett v. Rockland Fire & Marine Ins. Co., 65 Me. 374.

7 Bryant's Pond Steam Mill Co.

into shares. Persons who own these shares are the members of the corporation. Shares in such a corporation may be acquired in various ways, but in all cases there is a contract relation between the corporation and the shareholder or stockholder.

As we shall hereafter see at some length, shares of stock mav be acquired by virtue of a subscription therefor made before the corporation is formed, and expressly or impliedly accepted by the corporation after it is formed.<sup>8</sup> Or a subscription for shares may be both made and accepted after the corporation is In either case, when the subscription is accepted, so as to be binding upon both parties, the subscriber becomes a stockholder or member of the corporation, with all the rights, and subject to all the liabilities, arising out of such a relation.

Instead of acquiring shares of stock in a corporation by subscription therefor, a person may acquire them by purchase from the corporation after it has been formed, just as one may purchase any other property. A subscription for shares and a purchase of shares, as we shall hereafter see, are different contracts, and are in some respects subject to different rules.<sup>10</sup>

Shares of stock, with the resulting membership in the corporation, may also be acquired by transfer from the original or a subsequent holder. One of the incidents of a joint-stock corporation is that the shares therein, represented generally by certificates of stock, are transferable by the holders, without the consent of the other stockholders, or of the corporation, except in so far as such consent is implied as a matter of law from the nature of the corporation. When a corporation issues shares of its capital stock, it impliedly consents, and all the other stockholders impliedly consent, in the absence of express stipulation to the contrary, that the shares may at any time be transferred by the holder, and no further consent is necessary. The transferee of the shares, by reason of his ownership there-

v. Felt, 87 Me. 234, 47 Am. St. Rep. Mass. 82, 32 Am. St. Rep. 434. 323; Starrett v. Rockland Fire & And see post, §§ 439, 451. Marine Ins. Co., 65 Me. 374; Hudson Real Estate Co. v. Tower, 161 Mass. 10, 42 Am. St. Rep. 379, 156 8 Post, § 439(c).

<sup>9</sup> Post, § 439(b).

<sup>10</sup> Post. § 382.

of, becomes a member of the corporation, and assumes contract relations with it as such, in the place of the transferrer. Shares may be thus transferred by act of the parties, as by a sale, gift, or bequest, or by operation of law, as in the case of the holder's death, when they vest in his executor or administrator. transfer of shares will be considered at length in a subsequent chapter.11

## § 367. Corporations not having a capital stock.

There are many corporations, called "nonstock corporations," which have no capital stock divided into shares. Membership in such a corporation is acquired by a contract with the corporation, the mode of entering into which will vary according to the charter and by-laws of the particular corporation. Of this character are most of the stock and produce exchanges, and like bodies, incorporated social, literary, scientific, or political clubs or societies, mutual insurance and benefit companies, and the Membership in such corporations is usually evidenced by a certificate or policy of some kind issued by the corporation, and showing that the person named therein, or the holder, is entitled to the rights of membership. Certificates of membership in such corporations may be transferable, but they are not necessarily so. Whether they are or not, depends upon the charter and constitution or by-laws of the corporation, and the terms of the contract between it and its members. 12

Signing the constitution and by-laws of a nonstock corporation (as of an incorporated Odd Fellows' lodge), by the terms of which the signers agree to support the same, and pay all legal dues, etc., and are admitted to membership, constitutes the making of a valid contract of membership between the signer and the corporation, supported upon each side by a sufficient consideration.13

A contract of membership in mutual benefit and insurance

<sup>11</sup> Post, chapter xxiii.

<sup>12</sup> See American Live Stock Commission Co. v. Chicago Live Stock Exchange, 143 Ill. 210, 36 F., v. Hubbell, 2 Strob. (S. C.) 457, Am. St. Rep. 385, and other cases

hereafter cited.

<sup>49</sup> Am. Dec. 604.

companies, and like corporations, is usually effected by an application for membership in a particular form and its acceptance, and the issuance to the applicant of a policy or certificate of membership.<sup>14</sup> But this is not always necessary. Neither a formal application, nor the issuance of a policy or certificate, nor a formal acceptance of the application, where there is one, by the directors of the corporation, is necessary, ir the absence of an express provision therefor, if a completed contract of membership has in fact been otherwise made, and this may be shown by receipt and retention of fees, premiums, etc., or other conduct.<sup>15</sup> In every case, however, whether the contract be shown by formal writings or by conduct, the minds of the parties must have met, and there must be a completed contract of membership. 16

Compliance with provisions of charter, constitution, or by-laws. —In order that membership may be acquired in a nonstock corporation, the provisions of its charter, constitution, and valid by-laws must be complied with, except in so far as they may be and are waived.<sup>17</sup> When the valid by-laws of a corporation

Madison Mutual Ins. Co., 36 Wis. 599; Belleville Mutual Ins. Co. v. Van Winkle, 12 N. J. Eq. 333.

15 Burlington Voluntary Relief Department v. White, 41 Neb. 547, 43 Am. St. Rep. 701; Van Slyke v. Trempealeau County Farmers' Mutual Fire Ins. Co., 48 Wis. 683; Susquehanna Ins. Co. v. Perrine, 7 Watts & S. (Pa.) 348; Eilenberger v. Protective Mutual Fire Ins. Co., 89 Pa. St. 464; Cumberland Valley Mutual Protection Co. v. Schell, 29 Pa. St. 31.

16 Com. v. Massachusetts Mutual Fire Ins. Co., 112 Mass. 116; American Live Stock Commission Co. v. Chicago Live Stock Exchange, 143 Ill. 210, 36 Am. St. Rep. 385; Supreme Lodge of Pro-tection, Knights & Ladies of American Live Stock Commission Honor, v. Grace, 60 Tex. 569; Bal-timore & Ohio Employes' Relief change, 143 III. 210, 36 Am. St. Ass'n v. Post, 122 Pa. St. 579; Rep. 385; Matkin v. Supreme

14 See Burlington Voluntary Relation v. Supreme Lodge of lief Department v. White, 41 Neb. Knights of Honor, 82 Tex. 301, 27 547, 43 Am. St. Rep. 701; Fuller v. Am. St. Rep. 886.

Deduction by a railroad company of dues to an employes' relief association from the wages of an employe does not amount to an acceptance of the employe's application to the association for membership, or make him a member, a though the constitution and by-laws of the association authorize the railroad company to collect dues from members, it not appearing that the association has notified the company that the employe has been admitted to membership. Baltimore & Ohio Employes' Relief Ass'n v. Post, 122 Pa. St. 579, 9 Am. St. Rep. 147.

17 Belleville Mutual Ins. Co. v.

fix a particular mode of acquiring membership therein, membership, in the absence of a waiver, cannot be acquired in any other mode. Nor has a court of equity any power to compel the corporation to issue a certificate of membership to an applicant who has not complied with its by-laws.18

This point arose in an Illinois case, in which membership in the Chicago Live-Stock Exchange was claimed by a transferee of a certificate of membership therein. It appeared that the certificate had been transferred to the complainant by one who was a member, but that the complainant had not applied for membership. The by-laws of the corporation provided for admission to membership upon the written application of the applicant indorsed by two members, approved by seven votes of the board of directors, and upon payment of an initiation fee, or presentation of an unimpaired and unforfeited certificate of membership, duly transferred, and upon signing an agreement to abide by the rules, regulations, by-laws, and amendments thereto, of the corporation. It was held that the ownership of such a certificate did not constitute the complainant a member of the corporation, or entitle it to any rights as such, and that the only way in which it could avail itself thereof was by applying for membership in accordance with the by-laws, and tendering the certificate in lieu of the prescribed initiation fee, in case it should be admitted, or, in case its application

Lodge of Knights of Honor, 82 tution and by-laws of such an as-Tex. 301, 27 Am. St. Rep. 886. sociation make initiation indispen-

18 American Live Stock Commission Co. v. Chicago Live Stock Exchange, 143 Ill. 210, 36 Am. St. Rep. 385. See, also, McKane v. Adams, 123 N. Y. 609, 20 Am. St.

Rep. 785.

A by-law of a secret order or association which insures the lives of its members. making initiation enjoyment of the benefits attach-

sable to membership, and it is only upon the death of a member that his beneficiary is entitled to receive his insurance, the fact that a person's application for membership has been accepted, and his "proposition fee" paid, does not make him a member, or entitle his beneficiary to any insurance necessary to membership and the in the event of his death before he had been initiated as a member. ing thereto, is reasonable and Matkin v. Supreme Lodge of valid. And it has been held, Knights of Honor, 82 Tex. 301, 27 therefore, that where the consti-

should be rejected, then by selling the certificate to some other person desiring to become a member.19

Provisions in the by-laws of a corporation as to formal steps to be taken to acquire membership may be waived by the corporation, or it may be estopped to say that they have not been taken. In a late Nebraska case, therefore, where the relief department of a railroad company, in the nature of a mutual insurance company, organized for the benefit and protection of railroad employes in the case of sickness or death, placed an employe's name upon the roll of its membership at his solicitation, and deducted from his wages his assessments or dues, on the basis of membership, with knowledge of the fact that no formal application for membership had been made, and no physical examination had, as was required by its by-laws, it was held estopped from denying his membership in an action by his widow to recover a death benefit.20

Effect of fraud.—False and fraudulent misrepresentations as to material facts by an applicant for membership in a corporation, if not waived by the corporation with knowledge of the facts, will entitle it to rescind the contract of membership and exclude him, upon discovery of the fraud.<sup>21</sup> But, as a general rule, misstatements of fact do not amount to fraud, and are no ground for rescission, in the absence of a warranty, if they were made in good faith, and in the honest belief that they were true.22

19 American Live Stock Commission Co. v. Chicago Live Stock Exchance, 143 Ill. 210, 36 Am. St. Rep. 385.

20 Burlington Voluntary Relief Department v. White, 41 Neb. 547, 43 Am. St. Rep. 701.

21 Swett v. Citizens' Mutual Relief Soc., 78 Me. 541; Cobb v. Covenant Mutual Ben. Ass'n, 153 mass. 176 25 Am. St. Rep. 619; Briesenmeister v. Supreme Lodge Knights 619; Smith v. Baltimore & Ohio R. of Pythias of the World, 81 Mich. Co., 81 Md. 412.

22 Clapp v. Massachusetts Ben. Ass'n, 146 Mass. 519; Seiverts v. National Benev. Ass'n of City of Minneapolis, 95 Iowa, 710; Illinois Masons' Benev. Soc. v. Winthrop, 85 Ill. 537; Supreme Lodge of Knights of Pythias of the World v. Edwards, 15 Ind. App. 524.

Compare, in cases of warranty. Cobb v. Covenant Mut. Ben. Ass'n, 153 Mass. 176, 25 Am. St. Rep.

#### § 368. Power to admit members or exclude from membership.

In the absence of restrictions in its charter, a corporation has the implied or incidental power to admit new members. Thus, a statute incorporating certain persons and their associates as a historical society, and providing that they and their successors shall be capable of enjoying all privileges and franchises incident to a corporation, gives the corporation, as one of its incidental powers, the right to admit new members.23 And when the charter does not regulate or restrict the admission of new members, the whole matter is within the control of the corporation.<sup>24</sup> In the absence of charter or statutory restrictions, a corporation may determine who shall be admitted to membership, and how they shall be admitted. It may exclude any person whom it deems unfit for membership. deed, in the absence of restrictions, it may act arbitrarily, and exclude any persons it may see fit, and the courts have no power to interfere.25

 23 State v. Sibley, 25 Minn. 387.
 24 State v. Sibley, 25 Minn. 387; Diligent Fire Co. v. Com., 75 Pa. St. 291; Ellerbe v. Faust, 119 Mo.

Minors may be admitted as members of mutual benefit societies and other nonstock corporations, in the absence of provision to the contrary. Chicago Mutual Life Indemnity Ass'n v. Hunt, 127 Ill. 257.

Conditions as to age may be waived. McCoy v. Roman Catholic Mut. Ins. Co., 152 Mass. 272; Morrison v. Wisconsin Odd Fellow's Mut. Life Ins. Co., 59 Wis.

25 American Live Stock Commission Co. v. Chicago Live Stock Exchange, 143 Ill. 210, 36 Am. St. Rep. 385; McKane v. Adams, 123 N. Y. 609, 20 Am. St. Rep. 785; State v. Sibley, 25 Minn. 387; Varick v. Medical Society of New Jersey, 38 N. J. Law, 377; People v. Holstein Friesian Ass'n, 16 Abb. N. C. (N. Y.) 307, 41 Hun (N. Y.) 439; Ellerbe v. Faust, 119 Mo. 653.

See Hughes v. Farmers' Hay & Straw Market Ass'n, 20 Pa. St. 327; Blien v. Rand, 77 Minn. 110.

It is ordinarily for the corporation to determine the qualification and election of its members, and the mode of procedure is within its discretion. Varick v. Medical Society of New Jersey, 38 N. J. Law. 337.

Saloon keepers may be excluded by a by-law of a mutual benefit association. Ellerbe v. Faust, 119 Mo. 653.

A statute incorporating certain persons named, and all others "hereafter duly associated, as provided by the by-laws, to promote the best interests of owners of a certain breed of cattle, "and thereby the public generally," does not require the corporation to admit to membership any owner of such cattle who shall apply, or to register his cattle in its registry book. People v. Holstein Friesian Ass'n, 16 Abb. N. C. (N. Y.) 307, 41 Hun (N. Y.) 439.

In Blien v. Rand, 77 Minn. 110,

A corporation, however, has no power to exclude persons from membership in violation of its charter or enabling act, or to enact by-laws as to the admission or qualification of members, which conflict with its charter or the general law, or its articles of association, or which are contrary to public policy.26

#### II. Loss of Membership.

- § 369. In general.—A stockholder or member of a corporation may lose his membership in the following ways:
- (1) By transfer of his shares or membership, if, as is generally the case, they are transferable.
- (2) By forfeiture of his shares or membership when the power to forfeit the same has been conferred or is implied.

corporation, be restricted to persons of a certain nationality, where providing for the division the provision was not inconsistent with any statute.

26 When the charter of a corporation limits the membership to active members, a by-law authorizing the admission of merely contributing members is void. Diligent Fire Co. v. Com., 75 Pa. St. Ž91.

A corporation organized under a law authorizing the formation of corporations for the promotion of literary and scientific pursuits cannot pass valid by-laws limiting the qualification for membership to persons who are Irish, or of Irish parentage, and who are Roman Catholics, and providing for the appointment of a Roman Catholic bishop as spiritual di-rector. People v. Young Men's Father Mathew Total Abstinence Benev. Soc., 41 Mich. 67.

Under the Minnesota statutes incorporating the Union Depot Company of St. Paul for the benefit of railroads entering that city, to be such companies to subscribe for 248.

it was held that the right to mem- stock in said corporation, and probership in a corporation might, by hibiting any unjust discrimination a provision in its articles of in- against any company using or desiring to use the depot, and also shares, but fixing no price, it was held that, where five companies had become stockholders by purchasing shares at par, a company subsequently entering the city was entitled to become a stockholder by purchasing shares at par. St. Paul Union Depot Co. v. Minnesota & Northwestern R. Co., 47 Minn. 154.

It was also held that, where all the authorized stock was taken by railroad companies who were stockholders, they might be compelled to surrender so much as was necessary to entitle the incoming company to equal rights. Id.

If a statute gives persons the right to subscribe for stock in a corporation, and the corporation or its officers wrongfully refuse to receive their subscriptions, they may maintain an action against the corporation for damages. Union Bank v. McDonough, 5 La. 63; Walden v. Union Bank, 6 La. 248; Lallande v. Louisiana State Ins. Co., 9 La. 326.

It is otherwise if the board of diopen to all such roads then or rectors acted under an honest misthereafter constructed, authorizing take. Walden v. Union Bank, 6 La.

- (3) By surrender of his shares or withdrawal from membership, subject to the vested rights of other stockholders or members and of creditors.
  - (4) By disfranchisement or expulsion for sufficient cause. As to this mode of losing membership, the following rules may be stated:
    - (a) The power to expel members does not exist in the case of ordinary joint-stock corporations, and other corporations for pecuniary profit, unless it has been expressly conferred.
    - (b) But the power is inherent, subject to the following qualifications, in the case of corporations not for pecuniary profit:
    - (c) Unless such a corporation is expressly given the power to determine what causes shall justify expulsion of a member, it cannot expel except (1) for an infamous and indictable offense, upon a legal conviction thereof; (2) for an act or omission which is in violation of his duty to the corporation as a member; or (3) for an act or omission compounded of these two.
    - (d) By-laws relating to expulsion of members, when authorized, must be reasonable, and consistent with its charter and articles of association, and not contrary to law or public policy.
    - (e) To justify expulsion for an indictable offense, there must first be a legal conviction according to law.
    - (f) To justify expulsion for acts or omissions against the member's duties to the corporation, he must be first duly convicted before the corporation as a body, or before a select body, where the power to expel may be and has been delegated to such a body. And he is entitled to a fair hearing upon reasonable notice.
    - (g) If a member is wrongfully expelled, he has several remedies, namely: (1) Mandamus to compel the corporation to restore him to the rights of membership; (2) in some jurisdictions, but not in all, a suit in equity for an injunction and reinstate-

ment: or (3) in some jurisdictions, but not in all. an action to recover any damages sustained.

- (h) The courts, however, will not interfere until he has exhausted his remedies, by appeal or otherwise, within the corporation.
- (i) And the courts will not review the action of the corporation, if it did not exceed the powers conferred upon it by law.

#### § 370. Transfer of shares or membership-Stock corporations.

The usual mode in which a person ceases to be a member of a corporation is by a transfer of his shares or membership. As we shall see more at length in a subsequent chapter, it is generally an incident of joint-stock corporations that the shares of stock shall be transferable by the holder at any time, subject to the express provisions and regulations prescribed by the charter or articles of association and authorized by-laws of the corporation. And when a valid transfer is made, the transferrer ceases to be a member of the corporation, and the transferee takes his place.27 Shares of stock in a joint-stock corporation, however, may be made nontransferable by an express provision in the charter, or by a provision in the by-laws of the corporation, assented to by all the stockholders, provided there is nothing in the charter to prevent.<sup>28</sup>

Nonstock corporations.—Whether membership in a nonstock corporation is transferable depends upon the charter and bylaws of the corporation. If it is transferable, a valid transfer has the same effect as a transfer of shares in a stock corporation, —the transferrer is no longer a member, and the transferee takes his place.29

# Forfeiture of shares or membership.

Whether or not a joint-stock corporation, or other corporation

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<sup>27</sup> See post, § 563 et seq.
28 Herring v. Ruskin Co-opera-Commission Co. v. Chicago Live tive Ass'n (Tenn. Ch. App.) 52 S. Stock Exchange, 143 III. 210, 36 Am. St. Rep. 385.

for pecuniary profit, has the power to forfeit or sell the shares of a stockholder because of nonpayment of assessments thereon, depends upon whether such power has been expressly conferred upon it by the legislature or by agreement of the stockholders. Unless the power has been so conferred, it does not exist.<sup>30</sup> however, the power is conferred, and is properly exercised, the effect is to deprive the delinquent stockholder of his membership in the corporation, and he cannot afterwards claim any rights or be subjected to any liabilities as such.31

As we shall presently see, a member of a nonstock corporation may forfeit his right to remain a member, and be expelled or disfranchised, if he is guilty of conduct authorizing expulsion.32 In such a case, however, he must, as a rule, be expelled. A member of a corporation does not lose his membership, ipso facto, because of an act or default which is made a cause of forfeiture or expulsion, unless it is expressly so provided, but there must be proper action by the corporation expelling him.33

#### § 372. Surrender of shares or withdrawal from membership.

Members of a private corporation may surrender their shares at any time and withdraw from membership if they are not indebted to the corporation; and even when they are indebted

30 In re Long Island R. Co., 19 33 It was so held in an Alabama Wend. (N. Y.) 37, 32 Am. Dec. case where the constitution of a 429; Westcott v. Minnesota Minmedical society provided that, if

seq.

32 See post, § 373 et seg.

ing Co., 23 Mich. 145; In re St. annual dues should not be paid at Lawrence Steamboat Co., 44 N. J. a certain time, the defaulter Law, 529; Edgerton Tobacco Mfg. should forfeit his membership, and Co. v. Croft, 69 Wis. 256; post, should be duly notified thereof by \$493. 31 Small v. Herkimer Mfg. Co., requirement should be served each 2 N. Y. 330; Germantown Passen- year, and that, on reading the roll, ger Ry. Co. v. Fitler, 60 Pa. St. of members, any such defaulter 124, 100 Am. Dec. 546; Allen v. Montgomery R. Co., 11 Ala. 437; Mechanics' Foundry & Machine Co. v. Hall, 121 Mass. 272; Rutland & Burlington R. Co. v. Thrall, 35 Vt. 536. And see post, § 493 et membership. Medical & Surgical Soc. of Montgomery Co. v. Weatherly, 75 Ala. 248. See, also, State

to the corporation, they may be released by it, provided rights of other stockholders and of creditors are not violated by the release. This question will be considered at length in a subsequent chapter.34

#### § 373. Disfranchisement or expulsion of members.

(a) In general.—The power to declare a forfeiture and disfranchise or expel members may be expressly conferred upon a joint-stock corporation or other corporation for pecuniary profit by its charter or the general law in force at the time of its creation, or perhaps by a by-law assented to by all the stockholders or members.35 But the power does not exist in such corporations unless it is so conferred. It cannot be conferred by a by-law passed by a mere majority of the stockholders or members.36

 $\Lambda$  different rule, however, applies to nonstock corporations not organized for pecuniary profit, such as boards of trade, stock and produce exchanges, mutual benefit societies or associations, social, literary, and political clubs or societies, and Subject to any restrictions which may be contained in its charter, such a corporation has the implied or incidental power to disfranchise or expel a member, provided there is sufficient cause therefor, as will be explained in the following subdivisions. This power has been recognized and exercised from a very early period in the history of corporations.37

v. Trustees of Vincennes University, 5 Ind. 77. And see post, § 373(c).

Where a by-law of a religious society provided that any member should be dropped from the list if he should cease to worship regularly with the society, or fail to ·contribute to the support of its worship for one year, it was held that a member did not cease to be a member merely because of such omissions, and could not be experience of the such causes except by rows, 517; Lord Bruce's Case, 2 a vote of the society after a hearing. Gray v. Christian Society, 137 Mass. 329, 50 Am. Rep. 310.

34 Post, §§ 475, 476.

35 Post. § 493.

36 Westcott v. Minnesota Mining Co., 23 Mich. 145; In re Long Island R. Co., 19 Wend. (N. Y.) 37, 32 Am. Dec. 429; In re St. Lawrence Steamboat Co., 44 N. J. Law, 529; Edgerton Tobacco Mfg. Co. v. Croft, 69 Wis. 256; People v. Minong Mining Co., 33 Mich. 2. And see post. § 493.

Strange, 819; Evans v. Philadelphia Club, 50 Pa. St. 107; State v. Society for Support of Sick, 6

(b) Grounds for disfranchisement or expulsion.—A corporation has no power to disfranchise or expel a member arbitrarily, but there must be such cause therefor as to bring the case within the settled rules of law on the subject.38 There has been some conflict in the decisions as to what constitutes sufficient cause for expulsion. In the absence of express statutory or charter provision on the subject, the decided weight of authority is to the effect that the power is inherent, and may be exercised in three cases, and in three cases only, namely: (1) When an offense is committed which, although it has no immediate relation to a member's duty as such, is of so infamous a nature as to render him unfit for the society of honest men, and which is indictable at common law; (2) when the offense is a violation of his duty as a member of the corporation; <sup>39</sup> and (3) when the offense is of a mixed nature, being both against his duty as a member of the corporation, and also indictable at common law.40 "It appears to be well settled," said the supreme court of Wisconsin, "that when the charter of a corpora-

Desaus. (S. C.) 557; State v. Cham- cited in notes following. ber of Commerce of City of Mil-Soc., 2 Binn. (Pa.) 441, 4 Am. Dec. 453; Dickenson v. Chamber of 29 Wis. 45, 9 Am. Rep. 544; Albers v. Merchants' Exchange of City of St. Louis, 39 Mo. App. 583; Weber v. Zimmerman, 22 Md. 156; Taylor v. Edson, 4 Cush. (Mass.) 522; Burrows v. Massachusetts Medical Y.) 271. Society, 12 Cush. (Mass.) 402; Otto v. Journeymen Tailors' Pro-Cal. 308, 7 Am. St. Rep. 156; Poor of City of Philadelphia, 6 Peyre v. Mutual Relief Society of Serg. & R. (Pa.) 469; Leech v. French Zouaves, 90 Cal. 240; Harris, 2 Brewst. (Pa.) 571; Evans Meurer v. Detroit Musicians' Bev. Philadelphia Club, 50 Pa. St. nevo.ent & Protective Ass'n, 95 107.

Ohio Dec. 899; Smith v. Smith, 3 Mich. 451; and many other cases

38 Com. v. St. Patrick Benev. Soc., 2 Binn. (Pa.) 441, 4 Am. Dec. ber of Commerce of City of Milwaukee, 20 Wis. 63, 47 Wis. 670; Soc., 2 Binn. (Pa.) 441, 4 Am. Dec. People v. New York Commercial 453; Fuller v. Trustees of Acadesia, 18 Abb. Pr. (N. Y.) 271; People v. New York Board of Fire Chamber of Commerce of City of Underwriters. 54 How. Pr. (N. Y.) Milwaukee, 20 Wis. 63; State v. 240. 7 Hun (N. Y.) 248; Com. v. Georgia Medical Society, 38 Ga. Pailanthropic Soc., 5 Binn. (Pa.) 608. 95 Am. Dec. 408; and many 486; Com. v. St. Patrick Benev. lowing.

39 Whenever a member of a cor-Commerce of City of Milwaukee, poration is guilty of an offense 29 Wis. 45, 9 Am. Rep. 544; Albers which is "in direct contravention of the purposes for which the charter was obtained," he may be expelled. People v. New York Commercial Ass'n, 18 Abb. Pr. (N.

40 Com. v. St. Patrick Benev. Soc., 2 Binn. (Pa.) 441, 4 Am. Dec.

tion is silent upon the subject of expulsion, or grants the power in general terms, there are but three legal causes of disfranchisement: (1) Offenses of an infamous character indictable at common law. (2) Offenses against the corporator's duty to the corporation, as a member of it. (3) Offenses compounded of the two."41 If the conduct of a member comes within either of these causes, it is ground for expulsion, although it may not be expressly made so by the by-laws or rules of the corporation, and although they may specify some causes for expulsion.42

By-laws and regulations of corporation.—Corporations are frequently in express terms given the power to adopt by-laws and regulations for their government, or specifically for the expulsion of members. And the power exists, subject to limitations, even in the absence of an express provision therefor.<sup>43</sup> Corporations, therefore, other than joint-stock corporations, and other corporations for pecuniary profit, may always adopt reasonable by-laws, unless restricted by their charter or articles of association, declaring what shall constitute membership, and what shall operate as a forfeiture thereof, applicable to existing as well as future members, provided the by-laws are not contrary to law.44 Where the charter of a chamber of commerce organized for the purpose, inter alia, of establishing a high moral standard in conducting business transactions, etc., empowers it to suspend or expel members as it may see fit, a by-

41 Downer, J., in State v. Cham- Com. v. St. Patrick Benev. Soc., 2 ber of Commerce of City of Milwaukee, 20 Wis. 63, 72. And see
Dickenson v. Chamber of Commerce of City of Milwaukee, 29
Wis. 45, 9 Am. Rep. 544.

"On mature reflection it appears to me," said Chief Justice Tilghman in a Pennsylvania case, "that (Mass.) 522; Com. v. Union without an express power in the League of Philadelphia, 135 Pa. charter, no man can be disfran- St. 301, 20 Am. St. Rep. 870; and charter, no man can be disfran-chised, unless he has been guilty of some offense, which either af-

42 People v. New York Board of Fire Underwriters, 7 Hun' (N. Y.) 248, and cases hereafter referred

43 See post, chapter xxiv.

44 Taylor v. Edson, 4 Cush. cases hereafter cited.

A nonstock corporation may exfects the interests or good gov- pel members for violation of its ernment of the corporation or is by-laws, when authorized to punish indictable by the law of the land." infractions of its by-laws. Jacklaw providing for the suspension or expulsion of a member for failure to comply with the terms of any contract, whether verbal or written, is reasonable and valid, and authorizes expulsion for failure to perform a contract which is unenforceable by reason of the statute of frauds.45

When the power to expel members is not expressly conferred upon a corporation by its charter, so that it has such power only as is inherent, and exists at common law, the power cannot be exercised except when the member has been legally convicted of an infamous offense, or when he has committed some act tending to the destruction or injury of the corporation. And a by-law which vests in a majority of the members the power of expulsion for minor offenses is void.46 But where a corporation, such as a social club, for example, is expressly given the power to expel members, and to determine the causes which shall justify expulsion, and the manner of effecting the same, thus expressly vesting in a majority of the members the power to determine the causes for expulsion, a majority of the members may pass a by-law making minor offenses ground for expulsion, if they amount to disorderly conduct, or are injurious or hostile to the interests or objects of the association. It has been held, therefore, in a late Pennsylvania case, that a social club may, under such an express grant of power, pass a by-law providing for expulsion of members by a majority "for a willful infraction of the rules of the house, or of any by-law of the league, or for acts or conduct which they may deem disorderly, or injurious to the interests or hostile to the objects" of the association, and

son v. South Omaha Live Stock Ex- member for "fraudulent breach of change, 49 Neb. 687.

45 Dickenson v. Chamber of Commerce of City of Milwaukee, 29 Wis. 45, 9 Am. Rep. 544.

A produce exchange, incorporated for the purpose, among others, of inculcating "just and equitable principles of trade," and empowered to "make all proper and lawful 46 Evans v. Philadelphia Club, ed to "make all proper and lawful" 46 Evans v. Philadelphia Club, by-laws," and to expel members in 50 Pa. St. 107; Com. v. Union such manner as may be provided providing for expulsion of any see supra, this section.

contract, or of any proceedings inconsistent with just and equitable principles of trade." People v. New York Produce Exchange, 149

League of Philadelphia, 135 Pa. St. by its by-laws, may make a by-law 301, 20 Am. St. Rep. 870. And that under such a by-law a member may be expelled for being guilty of rude and ungentlemanly conduct in the club house, by charging a fellow member, without provocation, with acting like a blackguard.47

The fact that the charter of a corporation expressly gives it the power to expel members for certain causes does not impliedly exclude the power to expel for other causes which would be sufficient in the absence of an express provision, unless there is something to show that it was so intended.48

The power of a corporation to pass by-laws prescribing grounds for the expulsion of members, even when such power is expressly conferred, is not unlimited. The by-laws must be reasonable, and not contrary to law or public policy.49 New York case, where an incorporated medical society, having statutory authority to make by-laws and regulations relative to the admission and expulsion of members, fixed a tariff of fees, and a minimum salary to be received by any member who should be appointed to a public office in his character of physician, and passed a resolution to the effect that it would be dishonorable for any member to perform the duties named in the tariff for less than the tariff fees, and, in pursuance of a bylaw to that effect, expelled a member for violation of the regulation, it was held that the regulation was void as unreasonable and contrary to law and public policy, and the expulsion illegal,

adelphia, 135 Pa. St. 301, 20 Am. St. Rep. 870.

<sup>48</sup> Com. v. St. Patrick Benev. Soc., 2 Binn. (Pa.) 441, 4 Am. Dec. 453. And see Evans v. Club, 3 Luz. Leg. Obs. (Pa.) 205.

Benev. Soc., 2 Binn. (Pa.) 441, sions which will subject him to the 4 Am. Dec. 453; State v. Georgia penalty. People v. New York Prod-Medical Soc., 38 Ga. 608, 95 Am. uce Exchange, 149 N. Y. 401.

<sup>47</sup> Com. v. Union League of Phil- Dec. 408; Otto v. Journeymen lelphia, 135 Pa. St. 301, 20 Am. Tailors' Protective & Benevolent Union, 75 Cal. 308, 7 Am. St. Rep. 156; People v. New York Benev. Soc. of Operative Masons, 3 Hun (N. Y.) 361.

By-laws providing for expulsion of members must be consistent 49 People v. Medical Society of with the charter, and must state Erie County, 24 Barb. (N. Y.) 570; the causes of expulsion with such a Allnutt v. Subsidiary High Court, reasonable degree of certainty that

and that mandamus would lie to compel the corporation to restore the member.50

Of course by-laws providing for the expulsion of members of a corporation are void if they conflict with the charter of the corporation, or the general law under which it was formed.<sup>51</sup>

A charter or statutory provision giving a corporation authority to make rules, by-laws, and ordinances, and do everything needful for the good government and support of its affairs, gives the corporation no power to provide for the expulsion of members for causes which are insufficient under the settled principles of law on the subject.<sup>52</sup> A grant in general terms, in the charter of a corporation, of the power to suspend or expel members, gives no power to expel a member for causes not affecting the government of the corporation or accomplishment of its objects, and not amounting to an indictable offense.<sup>53</sup>

Particular cases.—Many cases have come before the courts for determination of the sufficiency of particular acts to justify expulsion, and it may be well to refer to them specifically.

It has been held that an incorporated chamber of commerce, board of trade, or other like institution, may disfranchise, expel, or suspend a member, in pursuance of a by-law, for refusal or failure to promptly perform a contract, even though the contract may be unenforceable because it is not in writing, as required by the statute of frauds;54 for violating a by-law pro-

50 People v. Medical Society of merce of City of Milwaukee, 20 Erie County, 24 Barb. (N. Y.) 570. Wis. 63.

could not be expelled for mere introit, 31 Mich. 458.

51 New York Protective Ass'n v. McGrath, 23 N. Y. 209.

Under a statute providing that corporations might prescribe suitable penalties for the violation of their by-laws, not exceeding in any case twenty dollars for any one offense, it was held that a member could not be expelled for mere in-

Under a by-law of a produce exfraction of a by-law. People v. change providing for expulsion of Fire Department of City of De-members for "willful violation of the charter or by-laws, or for <sup>52</sup> Com. v. St. Patrick Benev. fraudulent breach of contract, or Soc., 2 Binn. (Pa.) 441, 4 Am. Dec. for any proceedings inconsistent with just and equitable principles 53 State v. Chamber of Com- of trade, or for other misconduct," hibiting members from gathering in any public place in the vicinity of the exchange room, and forming a market, for the purpose of making any trade or contract for the future delivery of grain or provisions, before the time fixed for opening the exchange room for general trading, or after the time fixed for closing the same;55 for allowing rebates to customers contrary to the rules and regulations of the association;56 for making or reporting any false or fictitious purchases or sales, or acting in any way in bad faith, dishonestly, or dishonorably;57 or for obtaining goods under false pretenses.58

It has also been held that a member of a board of fire underwriters, organized to maintain uniformity in insurance rates among its members, may be expelled for charging lower rates than those fixed by the association; 59 that a physician who is a member of a medical society may be expelled for selling out his practice, and then resuming practice in the same locality to the purchaser's injury;60 or for holding himself out as prepared and willing to practice either as an allopath or homeopath, as might be desired by the patient, etc.;61 that a member of

a mere breach or nonperformance of a contract, unaccompanied by City of Chicago, 121 Ill. 412. any moral delinquency, is no cause for expulsion; but the by-law exand fair dealing, although it may although it is not of that specific and definite character of which the law, in an action between the parties, will take notice. People v. New York Produce Exchange, 149 N. Y. 401.

The fact that the contract is enforceable at law does not make it any the less a cause for expulsion under such a by-law. Id.

As to the power of the New York Stock Exchange to expel members, see Belton v. Hatch, 109 N. Y. 593. 55 State v. Milwaukee Chamber

of Commerce, 47 Wis. 670.

56 Jackson v. South Omaha Live Stock Exchange, 49 Neb. 687.

57 Pitcher v. Board of Trade of

<sup>58</sup> People v. New York Commercial Ass'n, 18 Abb. Pr. (N. Y.) 271. tends to conduct in respect to a it was so held in this case, alcontract, either in its inception or though the offense was not com-execution, or the failure to perform mitted within the local jurisdicit, which is inconsistent with just tion of the corporation, nor against a member thereof, the corporation fall short of actionable fraud, and having been formed inter alia, "to inculcate just and equitable principles in trade," and the offense being in direct contravention of such object.

59 People v. New York Board of Fire Underwriters, 7 Hun (N. Y.) 248, affirming 54 How. Pr. 240.

60 Barrows v. Massachusetts Medical Society, 12 Cush. (Mass.)

A medical society may discharge a member for gross immorality in a professional transaction. Barrows v. Massachusetts Medical Society, 12 Cush. (Mass.) 402.

61 Ex parte Paine, 1 Hill (N. Y.)

a trades union may be expelled for working, in violation of the by-laws of the union, for a person who does not pay wages weekly, or who employs nonunion men. 62

It has also been held in a number of cases that a member of a mutual benefit association or other corporation may be expelled for failure to pay legal dues, assessments, or fines, as required by his contract of membership, if there is an express provision therefor.63

A member of a mutual benefit association may be expelled if he fraudulently alters his certificate or a physician's bill, etc.,

62 Burns v. Bricklavers' Union N. C. (N. Y.) 20. But see Otto v. Journeymen Tailors' Protective Union, 75 Cal. 308, 7 Am. St. Rep. 156, and People v. New York Protective

Ann. 1098; Young v. Grand Lodge 3 Hun (N. Y.) 361.

of the Sons of Progress, 173 Pa. A by-law authorizing directors St. 302; Scheu v. Grand Lodge, of a corporation to fine or suspend Ohio Division, Independent Fora member for disorderly conduct esters, 17 Fed. 214; Hussey v. Galdoes not authorize suspension of lagher, 61 Ga. 86; Medical & Suramember for the nonpayment of gical Society of Montgomery Co. a fine imposed for violating a rule v. Weatherly, 75 Ala. 248; Sibley of the corporation, where he in yeard of Management of Carteret Club of Elizabeth 40 N. I. the fine Albers v. Merchants' teret Club of Elizabeth, 40 N. J. Law, 295; Karcher v. Supreme Lodge, Knights of Honor, 137 Mass. 371; Wheeler v. Connecticut Mut. Life Ins. Co., 82 N. Y. 543, 37

Am. Rep. 594; Whiteside v. Noyac Cottage Ass'n. 142 N. Y. 585. Compare Hibernia Fire Engine Co. v. Com., 93 Pa. St. 264; Diligent Fire Co. v. Com., 75 Pa. St. 291; People v. Fire Department of City of Detroit, 31 Mich. 458; People v. New York Benev. Soc. of Operative Masons, 3 Hun (N. Y.) 361.

But there must be an express provision therefor to authorize expulsion for nonpayment of a fine. Erd v. Bavarian National Aid & agreement, and collect them. Den-Relief Ass'n of City of Detroit, ver Chamber of Commerce & Board 67 Mich. 233.

There can be no expulsion for No. 1 of City of Brooklyn, 27 Abb. nonpayment of a fine which is different from that authorized by the by-laws. Meurer v. Detroit Mu-sicians' Benevolent & Protective Ass'n, 95 Mich. 451.

Benev. Soc. of Operative Masons, 3 Hun (N. Y.) 361.

State v. Stevedores & Longshoremen's Benev. Ass'n, 43 La.
Ann. 1098; Young v. Grand Lodge 3 Hun (N. Y.) 361.

of the corporation, where he in good faith contests the validity of the fine. Albers v. Merchants' Exchange of City of St. Louis, 39

Mo. App. 583.

A by-law providing that, if a member fails to pay dues for a year, he shall be deemed to have relinquished his membership, and may be excluded from the rooms of the association, and his certificate of membership shall be sold at auction, and any surplus of the proceeds be paid over to him, does not ipso facto terminate the membership of one whose dues are a year in arrear, nor is the remedy given for nonpayment of dues exclusive. The corporation, so long as he remains a member, may sue on his of Trade v. Green, 8 Colo. App. 420.

so as to increase the benefits secured thereby;64 or if he fraudulently pretends to be sick or disabled in order to obtain benefits, or draws relief after recovery;65 and it has been assumed that a member of such an association may be expelled for enlisting as a soldier in active service, contrary to the provisions of a by-law.66 A trustee may be expelled for fraudulently charging the corporation with money which he has not paid.67

It has also been held in a late case, as heretofore stated, that a member of a social club may be expelled for being guilty of rude and ungentlemanly conduct in the club house, by charging a fellow member, without provocation, with acting like a blackguard, where the charter of the club expressly allows a majority. of the members to determine the causes which shall justify expulsion, and they have passed a by-law providing for expulsion "for a willful infraction of the rules of the house, or of any by-law of the league, or for acts or conduct which they may deem disorderly, or injurious to the interests or hostile to the objects" of the club.68

On the other hand, it has been held that a member of a corporation (a social club) cannot be expelled for minor offenses, even in pursuance of a by-law, where the corporation is not expressly given the power to determine causes for expulsion, and that he cannot be expelled, therefore, under such circumstances, for striking another member, or using insulting language to him;69 that a person cannot be expelled for deviation from the by-laws or rules of the corporation prior to becoming a member; 70 that a member of a chamber of commerce, board

<sup>5</sup> Binn. (Pa.) 486.

<sup>65</sup> Society for Visitation of the Sick & Burial of Dead v. Com., 52 Pa. St. 125, 91 Am. Dec. 139. 66 Franklin Beneficial Ass'n v.

Com., 10 Pa. St. 357.
But is not such a by-law contrary to public policy? See In re Charter of David Mulholland Benev. Soc. of Manayunk, 10 Phila. (Pa.) 19.

<sup>67</sup> Com. v. Guardians of the Poor Erie County, 32 N. Y. 187.

<sup>64</sup> Com. v. Philanthropic Society, of City of Philadelphia, 6 Serg. & R. (Pa.) 469.

<sup>68</sup> Com. v. Union League of Philadelphia, 135 Pa. St. 301, 20 Am. St. Rep. 870. Compare cases referred to in note 75, infra.

<sup>69</sup> Evans v. Philadelphia Club, 50 Pa. St. 107. Compare Com. v. Union League of Philadelphia, 135 Pa. St. 301, 20 Am. St. Rep. 870.

<sup>70</sup> People v. Medical Society of

of trade, exchange, or similar corporation cannot be expelled for refusal or failure to submit a matter in dispute to arbitration after having commenced suit upon it;<sup>71</sup> for refusal to pay an award rendered in an arbitration, where the member protested against the arbitration on the ground that the association had no jurisdiction;<sup>72</sup> for selling a seat to which the managers have declared the member's title invalid;<sup>73</sup> that a member of a mutual benefit association or social club or society cannot be expelled under a by-law merely for villifying or defaming or privately quarreling with another member,<sup>74</sup> at least where the association is not expressly vested with the power to determine what causes shall justify expulsion;<sup>75</sup> or for refusal to take a sacrament in accordance with the forms and practice of a particular church or sect;<sup>76</sup> for defaming and injuring the society in taverns;<sup>77</sup> or for refusal to join in a labor strike.<sup>78</sup>

It has also been held that a physician cannot be expelled from a medical society for receiving for his services a less fee than that prescribed by the by-laws of the society;<sup>79</sup> or for advertis-

71 State v. Chamber of Commerce of City of Milwaukee, 20 Wis. 63.

<sup>72</sup> Savannah Cotton Exchange v. State, 54 Ga. 668.

73 People v. New York Cotton Exchange, 8 Hun (N. Y.) 216.

74 People v. Alpha Lodge No. 1 of Knights of Sobriety, Fidelity & Integrity, 13 Misc. Rep. (N. Y.) 677, 8 App. Div. 591; Evans v. Philadelphia Club, 50 Pa. St. 107; Com. v. St. Patrick Benev. Soc., 2 Binn. (Pa.) 441, 4 Am. Dec. 453. "The offense of villifying a member or a private quarrel," said Chief Justice Tilghman in the case last cited, "is totally unconnected with the affairs of the society, and therefore its punishment cannot be necessary for the good government of the corporation."

A member of a corporation cannot be expelled for defaming another member, unless the defamation was without any reasonable cause. Allnutt v. Subsidiary High Court of United States Ancient Order of Foresters, 62 Mich. 110.

75 Com. v. Union League of Philadelphia, 135 Pa. St. 301, 20 Am. St. Rep. 870.

<sup>76</sup> People v. St. Franciscus Ben. Soc., 24 How. Pr. (N. Y.) 216.

77 Com. v. German Society for Mutual Support & Assistance, 15 Pa. St. 251.

78 In People v. New York Benev. Soc. of Operative Masons, 3 Hun (N. Y.) 361, it was held that a member of a beneficial association could not be expelled under a by-law for working at a trade, and refusing to join a strike, as such a by-law was contrary to public policy. See, also, Otto v. Journeymen Tailors' Protective & Benevolent Union, 75 Cal. 308, 7 Am. St. Rep. 156. But see Burns v. Bricklayers' Union No. 1 of City of Brooklyn, 27 Abb. N. C. (N. Y.) 20.

other member, unless the defamaresponsible tion was without any reasonable Erie Co., 24 Barb. (N. Y.) 570.

ing a particular remedy;80 or for becoming surety on the official bond of a negro elected to office, "in opposition to the wishes of the entire respectable community," and becoming surety on the bonds of negroes charged with inciting a riot, etc. 81

It has also been held that a member of an incorporated religious society cannot be expelled for immorality, in the absence of provision therefor in its charter;82 that a member of an educational corporation cannot be expelled for disrespectful and contemptuous language towards his associates, and neglect of duty in not acting on committee.83 A member of a medical society or other corporation other than a political club or association cannot be expelled because his political views and acts as a politician are distasteful to the other members.84

A member of a corporation cannot be expelled under a bylaw or regulation of the corporation, unless the case comes strictly within its terms. Nor can a member be expelled in violation of a by-law.85 Where a corporation adopted, for the government of the debates of its members, Cushing's Manual, which prohibits censure of a member for speaking offensive words, if no notice was taken of them when they were spoken, and they were not written down until after the intervention of business after he had finished his speech, it was held that a member was unlawfully expelled for using offensive words which were not noticed or objected to until a subsequent meet-

so People v. Medical Society of of a member who shall be guilty of Erie Co., 32 N. Y. 187. an act whereby the reputation of

Evangelical St. Stephen's Church, turpitude, and does not authorize 53 N. Y. 103.

83 Fuller v. Trustees of Academic School in Plainfield, 6 Conn. 532.

84 State v. Georgia Medical Society, 38 Ga. 608, 95 Am. Dec. 408.

company providing for expulsion

81 State v. Georgia Medical So- the company may be injured, witciety, 38 Ga. 608, 95 Am. Dec. 408. nessed by any member of the com-82 People v. German United pany, applies only to acts of moral expulsion of a member for withholding from the company money which he claims he has no right to turn over to it, or for other transactions of a purely financial character between himself and a third 85 People v. American Institute person concerning the division of a of City of New York, 44 How. Pr. commission for a loan to the com-(N. Y.) 468. A by-law of a hook and ladder & Ladder Co., 61 N. J. Law, 507.

86 People v. American Institute

- —Disqualification for membership.—It has been held in some jurisdictions that a member of a corporation may be expelled because of original disqualification for membership.<sup>87</sup> In a New York case, however, it was held that a defect in a member's original qualifications for membership, and the fact that he procured his admission by false representations, could only be inquired into by quo warranto, and were no ground for his expulsion by resolution of the corporation.<sup>88</sup>
- —Good faith.—Expulsion of a member must be in good faith, and because of the act or conduct relied upon as the cause of expulsion. If a member is expelled nominally for an offense which would warrant his expulsion, but in reality for an offense which, by the rules or by-laws of the corporation, is punishable by a fine only, he will be reinstated by the courts.<sup>89</sup>
- —Waiver of cause of expulsion.—A corporation may waive the right to expel a member for violation of a by-law, or other acts in violation of his duty to the corporation, and if it consents to or acquiesces in an act, it cannot afterwards expel therefor.<sup>90</sup>
- (c) Mode of procedure to expel members.—Before a member of a corporation can be expelled merely on the ground that he has committed an indictable offense, "it is necessary that there should be a previous conviction by a jury, according to the law of the land."<sup>91</sup> When the offense is against the member's duty to the corporation, he may be expelled on trial and conviction by the corporation.<sup>92</sup>

of City of New York, 44 How. Pr. (N. Y.) 468.

<sup>87</sup> Reg. v. Saddlers' Co., 10 H. L. Cas. 404; Beesley v. Chicago Journeymen Plumbers' Protective & Benevolent Ass'n, 44 Ill. App. 278. And see Diligent Fire Co. v. Com., 75 Pa. St. 291.

88 Fawcett v. Charles, 13 Wend. (N. Y.) 473.

sº Otto v. Journeymen Tailors'
Protective & Benevolent Union, 75
Cal. 308, 7 Am. St. Rep. 156.

90 Harmstead v. Washington Fire Co., 1 Leg. Gaz. (Pa.) 392, wherein it was held, in effect, that a fire company could not expel a member for joining another company in violation of a by-law, where it acquiesced therein.

91 Com. v. St. Patrick Benev. Soc., 2 Binn. (Pa.) 441, 4 Am. Dec.

453.

92 Com. v. St. Patrick Benev. Soc., 2 Binn. (Pa.) 441, 4 Am. Dec. 453, and cases cited in the notes following.

A member of a corporation cannot be disfranchised or expelled without the agency of a tribunal competent to investigate the cause, and pronounce the sentence of the loss of the right to membership.93 The power to expel a member is primarily in the whole body of members as constituting or representing the corporation, and cannot be exercised by the directors or trustees, or other officers,94 unless there is some provision to the contrary in the charter of the corporation, or unless the whole body of members have, by a duly-adopted and valid bylaw or resolution, authorized in the particular jurisdiction, delegated the exercise of the power to the board of directors or some other select body. Some of the courts have held that there can be no such delegation of the power unless it is expressly authorized by the charter of the corporation;95 but the better opinion is to the contrary.96 The charter frequently

University, 5 Ind. 77; Gray v. delegate to its board of directors Christian Society, 137 Mass. 329, the power to expel members. 50 Am. Rep. 310; and cases in the notes following.

<sup>94</sup> State v. Chamber of Commerce of City of Milwaukee, 20 Wis. 63; Hassler v. Philadelphia Musical Ass'n, 14 Phila. (Pa.) 233; Weber v. Zimmerman, 22 Md. 156; Hibernia Fire Engine Co. v. Com.. 93 Pa. St. 264; Gray v. Christian Society, 137 Mass. 329, 50 Am. Rep. 310.

95 State v. Chamber of Commerce of City of Milwaukee, 20 Wis. 63; State v. Milwaukee Chamber of Commerce. 47 Wis. 670; Hibernia Fire Engine Co. v. Com., 93 Pa. St. 264; People v. Alpha Lodge No. 1 of Knights of Sobriety, Fidelity & Integrity, 13 Misc. Rep. (N. Y.) 677, 8 App. Div. 591.

In State v. Chamber of Commerce of City of Milwaukee, 20 Wis. 63, it was held that a provision in the charter of a corporation that it should have the power to admit as members such persons as it might see fit, and expel any member as it might see fit, did not by the charter.

93 State v. Trustees of Vincennes give the corporation the power to

96 People v. Board of Trade of Chicago, 45 Ill. 112; Pitcher v. Board of Trade of City of Chicago, Board of Trade of City of Chicago, 121 Ill. 412; People v. Women's Catholic Order of Foresters, 162 Ill. 78; Hussey v. Gallagher, 61 Ga. 86; People v. New York Commercial Ass'n, 18 Abb. Pr. (N. Y.) 271; White v. Brownell, 2 Daly (N. Y.) 329; People v. Fire Department of City of Detroit, 31 Mich. 458. See Green v. African Methodist Episcopal Society, 1 Serg. & R. (Pa.) 254.

In Hussey v. Gallagher, 61 Ga. 86, it was held that by-laws prescribing a trial before a select committee of members of an association, appointed by the president, and presided over by him, restricting witnesses to members, and prescribing that members should be dropped without trial if they should fail to pay fines, were not so unreasonable as to justify a court of equity in declaring them void, and enjoining their enforcement, where they were sanctioned confers upon a corporation the authority to delegate the power to expel members to a select board or committee or to certain officers, and of course, when this is so, the delegation of power is valid.97

In order that the action of a corporation in expelling a member for cause may be valid, it is essential, in the absence of a waiver, that there shall be a hearing or trial of the charge against him, with reasonable notice to him, and a fair opportunity to be heard in his defense.98 The notice must be per-

353; Southern Plank Road Co. v. Hixon, 5 Ind. 165; Medical & Surgical Society of Montgomery Co. v. Weatherly, 75 Ala. 248; People v. Mechanics' Aid Society, 22 Mich. 86; People v. Fire Department of City of Detroit, 31 Mich. 458; Erd v. Bavarian National Aid & Relief Ass'n of City of Detroit, 67 Mich. 233; Supreme Lodge of Ancient Order of United Workmen v. Zuhlke, 30 Ill. App. 98, 129 III. 298; Lysaght v. St. Louis Operative Stonemasons' Ass'n, 55 Mo. App. 538; Sibley v. Board of Management of Carteret Club of Elizabeth, 40 N. J. Law, People v. St. Franciscus Benev. Soc. of City of Buffalo, 24 How. Pr. (N. Y.) 216; People v. Medical Society of Erie County, 32 Wachtel v. Noah Y. 187; Widows' & Orphans' Benev. Soc., 84 N. Y. 28, 38 Am. Rep. 478; Peo-ple v. New York Benev. Soc. of was held that the courts could Operative Masons, 3 Hun (N. Y.) give no relief to a member of a

Order of Foresters, 162 Ill. 78; Protective Union, 118 N. Y. 101; Medical & Surgical Society of Delacy v. Neuse River Navigation Montgomery Co. v. Weatherly, 75 Co., 1 Hawks (N. C.) 274, 9 Am. Ala. 248; State v. Milwaukee Chamber of Commerce, 47 Wis. Beneficial Inst., 2 Serg. & R. (Pa.) 670; People v. Produce Exchange, 141; Com. v. German Society for 149 N. V. 401; Happler v. Produce Mutual Support & Assistance, 15 149 N. Y. 401; Haebler v. Produce Mutual Support & Assistance, 15 Exchange, 149 N. Y. '15; People Pa. St. 251; Riddell v. Harmony v. Musical Mutual Protective Fire Co., 8 Phila. (Pa.) 310; Dili-Union, 47 Hun, 273, 118 N. Y. 101; gent Fire Engine Co. v. Com., 75 Screwmen's Benev. Ass'n v. Benson, 76 Tex. 552; Com. v. Union League of Philadelphia, 135 Pa. St. Dorchester Mutual Fire Ins. Co., 201, 204 May 24 Pap. 270; Vange 121 Mass, 171; Karcher, v. Surface Pa. St. 291; Sleeper v. Franklin Lyceum, 7 R. I. 523; Mullen v. Dorchester Mutual Fire Ins. Co., 201, 204 May 24 Pap. 270; Vange 121 Mass, 171; Karcher, v. Surface Pa. St. 291; Sleeper v. Franklin Lyceum, 7 R. I. 523; Mullen v. Dorchester Mutual Fire Ins. Co., 201; Mass, 171; Karcher, v. Surface Pa. St. 291; Sleeper v. Franklin Lyceum, 7 R. I. 523; Mullen v. Dorchester Mutual Fire Ins. Co., 201; Mass, 171; Karcher, v. Surface Pa. St. 291; Sleeper v. Franklin Lyceum, 7 R. I. 523; Mullen v. Dorchester Mutual Support & Assistance, 18 v. Grand Lodge of Sons of Progress, 173 Pa. St. 302.

98 Fisher v. Keave, 11 Ch. Div. Society, 137 Mass. 329, 50 Am. Rep. 310; Grand Lodge Ancient Order United Workmen v. Brand, 29 Neb. 644; Von Arx v. San Francisco Gruetli Verein, 113 Cal. 377; Con-nelly v. Masonic Mutual Benefit Ass'n, 58 Conn. 553, 18 Am. St. Rep. 296.

A by-law authorizing expulsion summarily and without notice is unreasonable and void. People v. Fire Department of City of Detroit, 31 Mich. 458: and other cases above cited.

As to expulsion of an insane member, see Pfeiffer v. Weishaupt, 13 Daly (N. Y.) 161; Hellenberg v. District No. 1 of Independent Order of B'nai Berith, 94 N. Y. 580; Supreme Lodge of Ancient Order of United Workmen v. Zuhlke, 129 111. 298.

In Manning v. San Antonio Club,

sonal,<sup>99</sup> and not merely by posting the same on the premises of the corporation,<sup>100</sup> and it must reasonably inform the member of the charge against him.<sup>101</sup> Failure to serve notice is not excused by a mere change of the member's residence.<sup>102</sup> Failure to give any notice at all, or insufficiency of notice, may be waived and rendered immaterial by an appearance and failure to object.<sup>103</sup>

The trial or hearing and the notice thereof must be in accordance with the charter and by-laws or regulations of the corporation, or the expulsion will be wrongful.<sup>104</sup> If the mode of pro-

social club who was expelled therefrom without notice, where the by-laws did not require notice. This decision is clearly wrong and is directly contrary to the decision in every other case in which the question has arisen.

<sup>99</sup> Wachtel v. Noah Widows' & Orphans' Benev. Soc., 84 N. Y. 28, 38 Am. Rep. 478; Sibley v. Board of Management of Carteret Club of Elizabeth, 40 N. J. Law, 295; and other cases above cited.

100 Sibley v. Board of Management of Carteret Club of Elizabeth, 40 N. J. Law, 295.

101 Murdock's Case, 7 Pick. (Mass.) 303; Murdock v. Trustees of Phillips Academy, 12 Pick. (Mass.) 244; Allnutt v. Subsidiary High Court of United States Ancient Order of Foresters, 62 Mich. 110; Spilman v. Supreme Council of the Home Circle, 157 Mass. 131.

102 Wachtel v. Noah Widows' & Orphans' Benev. Soc., 84 N. Y. 28, 38 Am. Rep. 478.

103 Com. v. Pennsylvania Ben. Soc., 2 Serg. & R. (Pa.) 141; People v. Coachman's Union Benev. Ass'n of City of New York, 4 Misc. Rep. (N. Y.) 424; Levy v. Magnolia Lodge No. 29, I. O. O. F., 110 Cal. 309. Compare Downing v. St. Columbia's R. C. T. A. B. Soc., 10 Daly (N. Y.) 262.

A member, while insane, cannot waive notice in person. Supreme Lodge of Ancient Order of United Workmen v. Zuhlke, 129 Ill. 298.

104 Medical & Surgical Society of Montgomery Co. v. Weatherly, 75 Ala. 248; People v. Musical Mutual Protective Union, 47 Hun (N. Y.) 273; People v. New York Benev. Soc. of Operative Masons, 3 Hun (N. Y.) 361; People v. Alpha Lodge No. 1, Knights of Sobriety, Fidelity & Integrity, 13 Misc. Rep. (N. Y.) 677, 8 App. Div. 591; Fisher v. Keane, 11 Ch. Div. 353; Labouchere v. Earl of Wharncliffe, 13 Ch. Div. 346; Com. v. Guardians of the Poor of City of Philadelphia, 6 Serg. & R. (Pa.) 469; Com. v. Pike Beneficial Society, 8 Watts & S. (Pa.) 247; Washington Beneficial Society v. Bacher, 20 Pa. St. 425; Society for Visitation of the Sick & Burial of Dead v. Com., 52 Pa. St. 125; Young v. Grand Lodge Sons of Progress, 173 Pa. St. 302.

Where the charter of a corporation specially designates a particular meeting for the purpose of expelling members, or requires it to be called at a certain time, or in a particular mode, they cannot lawfully be expelled at any other meeting. Medical & Surgical Society of Montgomery Co. v. Weatherly, 75 Ala. 248; Weatherly v. Medical & Surgical Society of Montgomery Co. 76 Ala 567

Montgomery Co., 76 Ala. 567.

The fact that the charge upon which a member was expelled was preferred by an employe of the corporation, and not by another member, is immaterial. Albers v. Merchants' Exchange of City of St. Louis, 39 Mo. App. 583.

cedure is prescribed by the charter, it must be followed; but if no mode is thus prescribed, it may be fixed by the by-laws, provided they are reasonable and do not violate any rule of law or natural justice.105

The hearing must be conducted fairly and openly, and the body or person before whom it is had, and who are to decide, must be unprejudiced. 106 At the hearing the member is entitled to be represented by counsel, if he so desires. 107 And he is entitled to introduce evidence in his defense, and to crossexamine the witnesses against him. 108

As we have seen, failure to give notice is immaterial if the member appears.<sup>109</sup> And a hearing is not necessary if he admits the truth of the charge against him. 110

(d) Remedies for wrongful expulsion.—By the overwhelming weight of authority, if a member of a corporation is wrongfully expelled without sufficient cause, mandamus will lie to compel the corporation to restore him to membership, 111 unless

157 Mass. 128; People v. American Institute of City of New York, 44 How. Pr. (N. Y.) 468; Beesley v. Chicago Journeymen Plumbers' Protective & Benevolent Ass'n, 44 Ill. App. 278; Com. v. German Society for Mutual Support & Assistance, 15 Pa. St. 251.

To consider the question of expelling a member, notice must have been given to all the members of the corporation of the intention to consider the expulsion of the particular person. v. Zimmerman, 22 Md. 156.

106 State v. Adams, 44 Mo. 570; People v. Alpha Lodge No. 1, Knights of Sobriety, Fidelity & Integrity, 13 Misc. Rep. (N.Y.) 677, 8 App. Div. 591; Smith v. Nelson, 18 Compare Jackson v. South Omaha Live Stock Exchange, 49 Neb. 687, wherein it 453; Medical & Surgical Society was held that an order of the board of Montgomery Co. v. Weatherly, of directors expelling a member of 75 Ala. 248; State v. Georgia Medi-

105 State v. Trustees of Vincennes by-law was not subject to collateral University, 5 Ind. 77; Gray v. attack because of prejudice and dis-Christian Society, 137 Mass. 329, qualification of one of the directors, 50 Am. Rep. 310; Spilman v. Su-preme Council of the Home Circle, ing the trial of the charge before the board.

107 Murdock v. Trustees of Phillips Academy, 12 Pick. (Mass.) 244. 108 Murdock v. Trustees of Phillips Academy, 12 Pick. (Mass.)

He cannot be legally expelled on ex parte evidence. Fisher v. Keane, 11 Ch. Div. 353; La-bouchere v. Earl of Wharncliffe, 13 Ch. Div. 346; Sleeper v. Franklin Lyceum, 7 R. I. 523.

As to the effect of improperly excluding evidence, see Sperry's Appeal, 116 Pa. St. 391; Vaughn v. Herndon, 91 Tenn. 64.

109 Supra, this subdivision.

Appeal, 110 Maxey's Notes Cas. (Pa.) 441.

111 Com. v. St. Patrick Benev. Soc., 2 Binn. (Pa.) 441, 4 Am. Dec. a corporation for infraction of a cal Society, 38 Ga. 608, 95 Am.

there is some other adequate and complete remedy.<sup>112</sup> And the writ will also lie where one has been wrongfully expelled, even for sufficient cause, without a hearing, or without reasonable notice and an opportunity to be heard in his defense, or without compliance with the provisions of the charter and by-laws.<sup>113</sup>

In some jurisdictions it has been held that a suit in equity may be maintained by a member of a corporation to enjoin his wrongful expulsion, or compel reinstatement. According to the better opinion, however, since the remedy at law by mandamus to compel restoration to membership is generally adequate, a court of equity will not assume jurisdiction unless

Dec. 408; Savannah Cotton Exchange v. State, 54 Ga. 668; Evans v. Philadelphia Club, 50 Pa. St. 107; Black & White Smith's Society v. Vandyke, 2 Whart. (Pa.) 309, 30 Am. Dec. 263; Com. v. German Society for Mutual Support & Assistance, 15 Pa. St. 251; Sibley v. Board of Management of Carteret Club of Elizabeth, 40 N. J. Law, 295; People v. St. Franciscus Benev. Soc., 24 How. Pr. (N. Y.) 216; People v. Musical Mutual Protective Union, 118 N. Y. 101; State v. Chamber of Commerce of City of Milwaukee, 20 Wis. 63, 47 Wis. 670; State v. Adams, 44 Mo. 570; State v. Lipa, 28 Ohio St. 665; Allnutt v. Subsidiary High Court of United States Ancient Order of Foresters, 62 Mich. 110; Meurer v. Detroit Musicians' Benevolent & Protective Ass'n, 95 Mich. 451; Erd v. Bavarian National Aid & Relief Ass'n of City of Detroit, 67 Mich. 233; Otto v. Journeymen Tailors' Protective & Benevolent Union, 75 Cal. 308, 7 Am. St. Rep. 156; Lavalle v. Societe St. Jean Baptiste De Woonsocket, 17 R. I. 680.

Contra, Schmidt v. Abraham Lincoln Lodge, 84 Ky. 490.

It has been held, however, that mandamus to compel reinstatement will not lie after judgment in an action to recover damages for the expulsion, which is pending on appeal. State v. Lipa, 28 Ohio St. 665.

112 Harrison v. Simonds, 44 Conn. 318.

113 Delacy v. Neuse River Navigation Co., 1 Hawks (N. C.) 274, 9 Am. Dec. 636; Lysaght v. St. Louis Operative Stonemason's Ass'n, 55 Mo. App. 538; People v. Mechanics' Aid Society, 22 Mich. 86; Com. v. German Society for Mutual Support & Assistance, 15 Pa. St. 251; People v. Musical Mutual Protective Union, 47 Hun (N. Y.) 273, 118 N. Y. 101; and other cases in note 111. supra.

273, 118 N. Y. 101; and other cases in note 111, supra.

114 Leech v. Harris, 2 Brewst.
(Pa.) 571; Thomas v. Ellmaker, 1
Pars. Eq. Cas. (Pa.) 98; Olery v.
Brown, 51 How. Pr. (N. Y.) 92;
Albers v. Merchants' Exchange of City of St. Louis, 39 Mo. App. 583;
Smith v. Smith, 3 Desaus. (S. C.) 557; Altmann v. Benz, 27 N. J. Eq. 331; Hall v. Supreme Lodge,
Knights of Honor, 24 Fed. 450.

Under a Missouri statute authorizing a suit for injunction to prevent the doing of any legal wrong, where an action for damages will not afford an adequate remedy, it was held that a member of a corporation, on being wrongfully suspended for nonpayment of a fine, might sue to enjoin enforcement of the order of suspension, although he would have been reinstated on payment of the fine under protest, and might then recover it back in an action at law. Albers v. Merchants' Exchange of City of St. Louis, 39 Mo. App. 583.

there are peculiar circumstances rendering its interference necessary.115

A member of a corporation who has been cited to show cause why he should not be disfranchised for violation of its by-laws cannot maintain a suit, in advance of action by the corporation, to obtain an adjudication as to the validity of the by-laws, unless he can show that he will sustain irreparable injury. 116

And it is a well-settled rule that the courts will not act in reinstatement of a member of a corporation, claiming to have been wrongfully expelled, until he has pursued and exhausted all his remedies, by appeal or otherwise, within the organization itself; and it has been held that this is true, although the appellate body is a corporation of another state. 117

An expelled member of an incorporated beneficial association cannot have the sufficiency of the evidence upon which his expulsion was based or the regularity of the proceedings inquired into in a collateral action for the recovery of benefits alleged to be due him, where the expulsion was voted after notice, trial, and conviction in accordance with the provisions

City of Chicago, 80 Ill. 85; Baxter of Trade of City of Chicago, 86 Ill. 441; Gregg v. Massachusetts Medical Society, 111 Mass. 185, 15

Am. Rep. 24; White v. Brownell, 4 Abb. Pr. (N. Y.) 162. 116 Thomas v. Musical Mutual Protective Union, 121 N. Y. 45. 117 Zeliff v. Grand Lodge of New Peyre v. Mutual Relief Society of Jersey, Knights of Pythias, 53 French Zouaves, 90 Cal. 240; N. J. Law, 536; Ocean Castle, Oliver v. Hopkins, 144 Mass. 175; Knights of Golden Eagle, No. 11, v. Smith, 58 N. J. Law, 545, 59 N. J. Law, 198; Benson v. Screwmen's Daw, 150, Denson v. Screwmen's Cnamberlain v. Lincoln, 129 Mass. Benev. Ass'n, 2 Tex. Civ. App. 66; 70; Grosvenor v. United Society Screwmen's Benev. Ass'n v. Benson, 76 Tex. 552; Robinson v. Irish-American Benev. Soc., 67 Cal. 135; See, also, Bache v. Billingham American Benev. Soc., 67 Cal. 135; [1894] 1 Q. B. 107; Fisher v. Levy v. Magnolia Lodge No. 29, Keane, 11 Ch. Div. 353; LaI. O. O. F., 110 Cal. 297; Robinson bouchere v. Earl of Wharncliffe, v. Yates City Lodge No. 448, A. 13 Ch. Div. 346; Littleton v. Black-F. & A. M., 86 Ill. 598; Van Hou-

115 Fisher v. Board of Trade of ten v. Pine, 36 N. J. Eq. 133; Bauer v. Samson Lodge, Knights of Pythias, 102 Ind. 268; Harringv. Board of Trade of City of Chi-cago, 83 Ill. 146; Sturges v. Board ton v. Workingmen's Benev. Ass'n, 70 Ga. 340; People v. St. George's Society of City of Detroit, 28 Mich. 261; Reno Lodge No. 99, I. O. O. F. of Hutchinson, v. Grand Lodge, I. O. O. F. of Kansas, 54 Kan. 73; Jeane v. Grand Lodge, Ancient Or-der United Workmen, 86 Me. 434; Karcher v. Supreme Knights of Honor, 137 Mass. 368; Chamberlain v. Lincoln, 129 Mass.

of the charter and by-laws, and upon a charge thereby made a cause for expulsion.118

By the weight of authority, a member of a corporation who has been wrongfully expelled may maintain an action against the corporation to recover any damages which he may have sustained by reason of the expulsion, and is not restricted to his remedy to compel reinstatement.119

(e) Review by the courts.—The courts may review the action of a corporation in expelling a member, for the purpose of determining whether the cause of the expulsion was sufficient in law, whether the corporation proceeded in accordance with the law, upon reasonable notice to the member, and whether the hearing and expulsion was in good faith, and in compliance with its charter and by-laws, and, if the member was wrongfully expelled, he will be reinstated. 120 But the action of the corporation is conclusive, if it is within the powers conferred upon the corporation by its charter, and in accordance with the . law. "In the matter of expulsion, the society acts in a quasi judicial character, and so far as it confines itself to the exercise of the powers vested in it, and in good faith pursues the methods prescribed by its laws, such laws not being in violation of the laws of the land, or any inalienable right of the

309, 30 Am. Dec. 263.

St. Staneslaus Benev. Soc., 29 Mo. App. 337; Peo- the increase in value of the assets, ple v. Musical Mutual Protective he is entitled to interest on the Union, 118 N. Y. 101; Republican amount found due from the time Union, 118 N. Y. 101; Republican Newspaper Co. v. Northwestern Associated Press, 10 U. S. App. 72, 51 Fed. 377; Crosby Lumber Co. v. Smith, 3 U. S. App. 125, 51 Fed. 63.

Jean Baptiste de Woonsocket, 17 Society of French Zouaves, 90 Cal. 240.

fully excluded from a corporation, preceding, (c).

<sup>118</sup> Black & White Smith's So- and his interest therein declared ciety v. Vandyke, 2 Whart. (Pa.) forfeited, and in an action for damages he recovers the value of his 119 Ludowiski v. Polish Roman interest at the time it was taken Koska from him, including the profits and he was excluded. Crosby Lumber Co. v. Smith, 3 U. S. App. 125, 51 Fed. 63.

120 Otto v. Journeyman Tailors' Contra, Lavalle v. Societe Saint Protective & Benevolent Union, 75 Cal. 308, 7 Am. St. Rep. 156; Sa-R. I. 685, Peyre v. Mutual Relief vannah Cotton Exchange v. State, 54 Ga. 668; State v. Georgia Medical Society, 38 Ga. 608, 95 Am. Dec. When a shareholder is wrong- 408; and cases in the subdivision

member, its sentence is conclusive, like that of a judicial tribunal."121

121 Otto v. Journeyman Tailors' Protective & Benevolent Union, 75 Cal. 308, 7 Am. St. Rep. 156. See, Am. Dec. 263; Leech v. Harris, 2 also, Com. v. Pike Beneficial Soc., Brewst. (Pa.) 571; Com. v. Union 8 Watts & S. (Pa.) 250; Burt v. League of Philadelphia, 135 Pa. Grand Lodge, Free & Accepted St. 301, 20 Am. St. Rep. 870; Levy Masons, 44 Mich. 208; Robinson v. Yates City Lodge No. 448, A. F. & A. M., 86 Ill. 598; Pitcher v. Board of Trade of City of Chicago, 121 App. 613, 136 Ill. 185; Connelly v. Masonic Mut. Ben. Ass'n, 58 Conn. Lodge No. 5, Independent B'nai B'rith. v. Lodge No. 7, Independent Order v. Herndon, 91 Tenn. 64; Man-B'nai B'rith, 65 Md. 236; People v. ning v. San Antonio Club, 63 Tex. Board of Trade of Chicago, 80 Ill. Sick & Burial of Dead v. Com., 52 N. Y. 401. Pa. St. 125, 91 Am. Dec. 139:

Black & White Smith's Society v. Vandyke, 2 Whart. (Pa.) 309, 30 v. Magnolia Lodge No. 29, I. O. O. F., 110 Cal. 297; Supreme Council of Order of Chosen Friends v. Garrigus, 104 Ind. 133, 54 Am. Rep. Ill. 412; High Court, Independent 298; Woolsey v. Independent Or-Order of Foresters, v. Zak, 35 Ill. der of Odd Fellows, Lodge No. 23, 61 Iowa, 492; Gregg v. Massachusetts Medical Society, 111 Mass. 552, 18 Am. St. Rep. 296; Anacosta 185, 15 Am. Rep. 24; Gray v. Chris-Tribe No. 21, Improved Order of tian Society, 137 Mass. 329, 50 Red Men, v. Murbach, 13 Md. 91, Am. Rep. 310; Spilman v. Supreme 71 Am. Dec. 625; District Grand Council of Home Circle, 157 Mass. Or- 128; Burbank v. Boston Police Re-Jedidjah lief Ass'n, 144 Mass. 434; Vaughn 166, 51 Am. Rep. 639; People v. 134; Society for Visitation of the New York Produce Exchange, 149

## CHAPTER XX.

### CAPITAL STOCK AND SHARES OF STOCK.

- I. NATURE OF CAPITAL STOCK AND SHARES OF STOCK.
  - § 374. In general.
    - 375. "Capital stock," "capital," "stock."
  - , 376. Shares of stock.
    - 377. Liability of shares of stock to execution, attachment, garnishment, etc.
    - 378. Certificates of stock.
    - 379. Conversion of stock.
- II. ISSUE OF STOCK AND PAYMENT THEREFOR.
  - § 380. In eneral.
    - 381. Power of corporation to create and issue stock.
    - 382. How stock may be issued.
    - 383. Payment for stock in general.
    - 384. Payment in property, labor, or services.
    - 385. Payment in notes, bonds, mortgages, etc.
    - 386. Issue of stock in payment of debts.
    - 387. Pledge of stock by corporation.
    - 388. Right of existing stockholders to preference on issue of stock.
- III. WATERED OR FICTITIOUSLY PAID UP STOCK.
  - § 389. In general.
    - 390. Power of corporation in absence of express charter, statutory, or constitutional provisions.
    - 391. Special charter, statutory, or constitutional provisions.
    - 392. Valuation of property, labor, or services.
    - 393. Effect of issue of, or agreement to issue, watered stock.
    - 394. Effect as against the state.
    - 395. Effect as against the corporation itself.
    - 396. Effect as against the subscribers or purchasers.
    - 397. Effect as against dissenting stockholders.
    - 398. Effect as against stockholders participating, consenting, or acquiescing.
    - 399. Effect as against transferees.

- 400. Issue to directors or other officers.
- 401. Effect as against creditors.
- IV. Assessments upon Stockholders or Members after Payment in Full.
  - § 402. In general.
    - 403. Right to levy assessments.
    - 404. Power conferred by charter, statute, or agreement.
  - V. AMOUNT OF CAPITAL STOCK, AND INCREASE OR REDUCTION THEREOF.
    - § 405. In general.
      - 406. Amount of original capital stock.
      - 407. Increase and overissue of stock.
      - 408. Rights and remedies of existing stockholders with respect to new stock.
      - 409. Sale of new stock by corporation.
      - 410. Liabilities arising out of increase of stock.
      - 411. Reduction of capital stock.
      - 412. Increase or reduction of number of shares, or their par value.
- VI. PREFERRED OR GUARANTIED STOCK; INTEREST BEARING STOCK; SPECIAL STOCK.
  - § 413. In general,
    - 414. Preferred or guarantied stock defined.
    - 415. Power to issue preferred stock.
    - 416. Effect of unauthorized issue or agreement to issue.
    - 417. Rights and remedies of preferred stockholders.
    - 418. Liabilities of preferred stockholders.
    - 419. Rights of common stockholders.
    - 420. Interest bearing stock.
    - 421. Special stock under Massachusetts statute.
- VII. BONDS, ETC., CONVERTIBLE INTO STOCK, AND STOCK CONVERTIBLE INTO BONDS, OR LAND, ETC.
  - § 422. In general.
- VIII. ISSUE AND CANCELLATION OF CERTIFICATES OF STOCK; LOST CERTIFICATES.
  - § 423. In general.
    - 424. Power to issue certificates, and validity of certificates.
    - 425. Right to certificates, and remedies for refusal to issue the same.
    - 426. Rights and remedies in case of loss of certificates.
    - 427. Cancellation of certificates.

- IX. RIGHTS AND LIABILITIES ARISING OUT OF ISSUE OF FICTITIOUS CER-TIFICATES OF STOCK.
  - § 428. In general.
    - 429. Overissue of stock is void.
    - 430. Liability of corporation in damages.
    - 431. Authority of officer or agent issuing certificate.
    - 432. Forged certificate.
    - 433. Certificates signed in blank.
    - 434. Stolen certificates.
    - 435. Persons who are entitled to relief.
    - 436. Remedies of the corporation.
      - I. NATURE OF CAPITAL STOCK AND SHARES OF STOCK.
- § 374. In general.—The "capital stock" of a corporation is the amount subscribed and paid in or secured to be paid in by the shareholders, and upon which the corporation is to conduct its operations, as distinguished from its "capital," which term properly means its actual property or estate. The capital stock remains the same, until changed by or under legislative authority, however much the capital may increase or decrease.
  - A share of the capital stock of a corporation is the interest or right which the owner has in the corporation,—the right to participate, according to his interest, in the management of the corporation, in its surplus profits on a division, and altimately, on its dissolution, in the assets remaining after payment of its debts.
    - (a) Shares of stock are incorporeal personal property.
    - (b) They are not chattels, although in some jurisdictions they are held to be within the words "goods, wares, or merchandises" in the statute of frauds.
    - (c) They are in the nature of choses in action, but they are not choses in action. Nor are they "credits," "money," "securities," or "securities for money."
    - (d) The husband's rights in shares of stock owned by his wife are the same as in the case of choses in action.
    - (e) Being intangible, shares of stock, like choses in action, are not subject to execution, nor are they subject to attachment or garnishment, unless made so, as they now are in many jurisdictions, by statutory provision. Their situs for this purpose is the residence of the corporation, and not elsewhere.

A certificate of stock is not the stock itself, but merely evidence of the rights of the person named therein as a stockholder. In the absence of provision or agreement to the contrary, it is not necessary to constitute one a stockholder.

Shares of stock, although intangible, may be made the subject of an action of trover to recover damages for their conversion.

# § 375. "Capital stock," "capital," "stock."

The term "capital stock," properly speaking, signifies the amount subscribed and paid in or secured to be paid in by the shareholders of a corporation, either in money, or in property, labor, or services, in the organization of the corporation or afterwards, and upon which it is to conduct its operations, and does not mean, necessarily, the assets of the corporation. The amount of the capital stock is fixed by the charter or statute by or under which the corporation is created, or by the articles or certificate of association or incorporation, and always remains the same, unless it is increased or reduced by or under legislative authority,2 however much the assets or capital of the corporation may be increased by accumulation of profits or enhancement in the value of property, or reduced by losses or decrease of values.3

er's Cas. 851; Commercial Fire Ins. 97, 60 Am. Rep. 429, 2 Keener's Co. v. Board of Revenue of Montgomery County, 99 Ala. 1, 42 Am. St. Rep. 17; Williams v. Western In Canfield v. Morristown Fire Union Tel. Co., 93 N. Y. 162, 2 Ass'n, 20 N. J. Law, 195, 1 Keen-Cum. Cas. 209; People v. Commis-

1 "Strictly, the capital stock of a Storage Co. v. State Board of Ascorporation is the money contributed by the corporators to the capital, and is usually represented by shares issued to subscribers to the stock on the initiation of the corporate enterprise." Christensen v. Lawrence Furnace Co., 49 Ohio St. Eno, 106 N. Y. 97, 60 Am. Rep. 102; Wells v. Green Bay & Mississippi Canal Co., 90 Wis. 442; See, also, Canfield v. Morristown Fire Ass'n, 23 N. J. Law, 195, 1 Keener's Cas. 845; Burrall v. Bushwick R. Co., 75 N. Y. 211, 1 Keener's Cas. 851; Commercial Fire Ins. corporation is the money contrib- sessors, 56 N. J. Law, 389; Trades-

Cas. 1240; and other cases in note

er's Cas. 845, it was said: sioners of Taxes & Assessments phrase 'capital stock,' as employed for City and County of New York, in acts of incorporation, is never 23 N. Y. 192; American Pig Iron that I am aware, used to indicate

The term "capital" applied to corporations is often used interchangeably with "capital stock," and both are frequently used to express the same thing,—the property and assets of the corporation,-but this is improper. The capital stock of a corporation, as we have just seen, is the amount subscribed and paid in by the shareholders, or secured to be paid in, and upon which it is to conduct its operations; and the amount of the capital stock remains the same, notwithstanding the gains or losses of the corporation. The term "capital," however, properly means, not the capital stock, in this sense, but the actual property or estate of the corporation, whether in money or property. As was said in a New York case, "it is the aggregate of the sum subscribed and paid in, or secured to be paid in, by the shareholders, with the addition of all gains or profits realized in the use and investment of those sums, or, if losses have been incurred, then it is the residue after deducting such It follows that a corporation's capital may be many losses,"4 times greater than its capital stock, and it is this which makes the shares of stock of a corporation worth more on the market than their par value. Or a corporation with a large capital stock may have lost all its property, and may therefore have no capital, so that its shares will have no market value at all.

The term "stock" is sometimes used in the same sense as "capital stock."5 Ordinarily, however, it is used to designate, not

tutes the 'capital stock' of the com- 1240. pany. The value of the stock may

the value of the property of the County of New York, 23 N. Y. company. It is very generally, if 192, 219. "The capital of a cornot universally, used to designate poration consists of its funds, see the amount of capital to be care capital and appropriate conditions." the amount of capital to be con- curities, credits and property of tributed by the stockholders for whatever kind which it possesses." purposes of the corporation. The Christensen v. Eno, 106 N. Y. 97, amount thus contributed consti- 60 Am. Rep. 429, 1 Keener's Cas.

See, also, Canfield v. Morrisbe greatly increased by surplus town Fire Ass'n, 23 N. J. Law, 195, profits or be diminished by losses, 1 Keener's Cas. 845; Tradesman but the amount of the capital stock Publishing Co. v. Knoxville Car remains the same. The funds of Wheel Co., 95 Tenn. 634, 49 Am. the company may fluctuate. Its St. Rep. 943, 954; Wells v. Green capital stock remains invariable, Bay & Mississippi Canal Co., 90

Taxes & Assessments for City & Of Taxes & Assessments for City

the capital stock in the hands of the corporation, but the shares of the capital stock in the hands of the individual shareholders or stockholders, and this meaning should be given unless there is something to show a contrary intent.6

#### § 376. Shares of stock.

(a) In general.—A share of the capital stock of a corporation may be defined as the interest or right which the owner, who is called the "shareholder" or "stockholder," has in the management of the corporation, and in its surplus profits, and, on a dissolution, in all of its assets remaining after the payment of its debts.<sup>7</sup> It was said in a New York case that "the right which a shareholder in a corporation has by reason of his ownership of shares, is a right to participate according to the amount of his stock in the surplus profits of the corporation on a division, and ultimately on its dissolution, in the assets remaining after payment of its debts;"8 but this definition ignores the interest which a shareholder has in the management of the cor-

551, 556.

6 Lockwood v. Town of Weston, 61 Conn. 211. See ante, § 286 (d),

<sup>7</sup> See Fisher v. Essex Bank, 5 Gray (Mass.) 373, 1 Cum. Cas. 664, 2 Keener's Cas. 1080; Oakbank Oil Co. v. Crum, 8 App. Cas. 65; Burrall v. Bushwick R. Co., 75 N. Y. 211, 1 Keener's Cas. 851; Plimpton v. Bigelow, 93 N. Y. 592, 1 Keener's Cas. 855; Jones v. Concord & Montreal R. Co., 67 N. H. 234, 68 Am. St. Rep. 650; Neiler v. Kelley, 69 Pa. St. 403; Commercial Fire Ins. Co. v. Board of Revenue of Montgomery County, 99 Ala. 1, 42 Am. St. Rep. 17; Forbes v. Memphis, El Paso & Pac. R. Co., 2 Woods, 323, Fed. Cas. No. 4,926; Gibbons v. Mahon, 136 U. S. 549; Field v. Pierce, 102 Mass. 253; Union Nat. Bank of Chicago v.

& County of New York, 23 N. Y. 1 Keener's Cas. 33; Jones v. Davis, 192, 220; Burr v. Wilcox, 22 N. Y. 35 Ohio St. 474; Barksdale v. Fin-Brightwell v. Mallory, 10 Yerg. (Tenn.) 196.

> 8 Plimpton v. Bigelow, 93 N. Y. 592, 1 Keener's Cas. 855.

"The capital stock is that money, or property, which is put into a single corporate fund, by those, who by subscription therefor, become members of the corporate That fund becomes the property of the aggregate body only. A share of the capital stock, is the right to partake, according to the amount put into the fund, of the surplus profits of the corporation; and ultimately on the dissolution of it, of so much of the fund thus created, as remains unimpaired, and is not liable for Byram, 131 Ill. 92; Button v. Hoff-man, 61 Wis. 20, 50 Am. Rep. 131, Burrall v. Bushwick R. Co., 75 N. 1 Cum. Cas. 38, 1 Smith's Cas. 33, Y. 211, 1 Keener's Cas. 851. poration. "The right," said Chief Justice Shaw, "is, strictly speaking, a right to participate, in a certain proportion, in the immunities and benefits of the corporation; to vote in the choice of their officers, and the management of their concerns; to share in the dividends of profits, and to receive an aliquot part of the proceeds of the capital, on winding up and terminating the active existence and operations of the corporation."9

It follows from the nature of a share of stock, that the owner thereof is not the owner nor entitled to the possession of any definite portion of the assets of the corporation. The share is not a part of the assets. It is intangible,—a mere right to participate,—and is not capable of manual delivery. son may be the owner of shares of the stock of a corporation, and he may compel the corporation to deliver to him evidence of his right, but he cannot compel it to deliver to him the shares; and it follows that an action cannot be maintained for its refusal to do so.10

Since shares of stock are intangible and incapable of seizure and manual delivery, replevin will not lie to recover shares of stock, as distinguished from the certificate.\*

(b) Shares of stock as "personal property."—Although a share of stock is an "incorporeal intangible thing,"11 it is property; and it is now well settled that it is personal property, although the property of the corporation, in which the shareholder is beneficially interested, may consist chiefly or wholly of real estate.12 It is "incorporeal personal property."13

9 Fisher v. Essex Bank, 5 Gray (Mass.) 373, 1 Cum. Cas. 664, 2 Keener's Cas. 1080.

10 Burrall v. Bushwick R. Co., 75 N. Y. 211, 1 Keener's Cas. 851.

\*Ashton v. Heydenfeldt, 124 Cal.

But replevin will lie to recover a certificate of stock. See post. §

Kelley, 69 Pa. St. 403, 407.

infra.

13 Williams, Pers. Prop. 191; Allen v. Pegram, 16 Iowa, 163.

The franchise of exercising the rights of a stockholder was held to be "property," within a statute providing for service of process upon nonresident defendants by publication "in all actions at law or in equity, which have for their immediate object the enforcement 11 Sharswood, J., in Neiler v. or establishment of any lawful right, claim or demand to or 12 See the cases cited in note 15, against any real or personal property within the jurisdiction of the

It was at one time held in some jurisdictions that shares of stock in a canal company or other corporation whose property consisted of real estate were real property,14 but there are now statutory provisions to the contrary in these jurisdictions, or else the decisions to this effect have been overruled. And in the other jurisdictions in which the question has arisen it has been repeatedly held, and independently of any statute, that shares in all corporations, although they may own land, are personal and not real property. 15 This necessarily follows from the fact that the property of a corporation does not belong, in law, to the stockholders, but to the corporation as a distinct legal entity or artificial person, 16 and the right of the stockholder is merely the right to participate in the management of

erty" within the state, within the meaning of a statute authorizing jurisdiction of a nonresident defendant to be acquired by publication when he has property within the state. National Bank of New London v. Lake Shore & Michigan Southern Ry. Co., 21 Ohio St. 221; Jellenik v. Huron Copper Mining Co., 177 U. S. 1, reversing 82 Fed.

Shares of stock will pass under a conveyance, or devise and bequest, of all the grantor's or testator's "property, real and personal." Feckheimer v. National Exchange Bank of Norfolk, 79 Va.

14 Price v. Price's Heirs, 6 Dana (Ky.) 107; Copeland v. Copeland, 7 Bush (Ky.) 349; Welles v. 7 Bush (Ky.) 349; Welles v. Cowles, 2 Conn. 567; Coombs v. Jordan, 3 Bland Ch. (Md.) 284, 22 Am. Dec. 236. And see Meason's

clared its shares to be real prop- 16 Ante, § 6(c).

court." Smith v. Pilot Mining Co., erty. See Cooper v. Swamp Canal Co., 2 Murph. (N. C.) 195.

A nonresident shareholder in a domestic corporation has "property" within the state, within the State, within the State, within the state. 847; Humble v. Mitchell, 11 Adol. & E. 205, 1 Cum. Cas. 602; Russell v. Temple, 3 Dane, Abr. 108, 1 Smith's Cas. 23; Tippets v. Walk-er, 4 Mass. 595; Sargent v. Franklin Ins. Co., 8 Pick. (Mass.) 90, 19 Am. Dec. 306; Johns v. Johns, 1 Ohio St. 350; Mattingley v. Roach, 84 Cal. 207; South Western R. Co. v. Thomason, 40 Ga. 408; Baldwin v. Canfield, 26 Minn. 61; Weyer v. Second Nat. Bank of Franklin, 57 Ind. 198; Manns v. Brookville Nat. Bank, 73 Ind. 243; Seward v. City of Rising Sun, 79 Ind. 351; Tregear v. Etiwanda Water Co., 76 Cal. 537, 9 Am. St. Rep. 245; Arnold v. Ruggles, 1 R. I. 165; Dyer v. Osborne, 11 R. I. 321, 23 Am. Rep. 460; Saup v. Morgan, 108 III. 326; Allen v. Pegram, 16 Iowa, 163; McKean v. County of Northampton, 49 Pa. St. 519, 88 Am. Dec. 515; North v. Forest, 15 Conn. 400; Estate, 4 Watts (Pa.) 341; Tom-linson v. Tomlinson, 9 Beav. 459.

There have been instances in which the charter of a corpora-tion, or some other statute, has, for the purposes of inheritance, de-clared its shares to be real propthe corporation, in any dividends which may be declared from profits, and ultimately in the distribution of what remains of its assets, on dissolution, after payment of its debts.<sup>17</sup>

In accordance with this doctrine, it has been held that shares of stock, although the property of the corporation consists of land, are personal property for the purpose of determining their situs for the purposes of taxation,18 and a tax thereon is a personal tax. 19 For some purposes, however, the situs of shares of stock is at the domicile of the corporation, and not at the domicile of the stockholder, as in the case of personal property generally.\* It has also been held that shares of stock are personal property for the purposes of sale<sup>20</sup> or mortgage;<sup>21</sup> that they are not land, nor an interest in land, within the clause of the statute of frauds requiring a memorandum in writing in the case of contracts for the sale of land or an interest therein; 22 that, on the death of the owner, they go, at common law, to his executor or administrator, as personalty, and not to his heirs as realty, and will pass as personalty under the statutes of descent and distribution;23 that a will disposing of shares in a corporation owning land need not be executed in accordance with the provisions of the statute of frauds relating to wills devising land;24 that a prohibition against loans by a corporation on real estate security does not prohibit loans on the security of stock in a

<sup>&</sup>lt;sup>17</sup> See supra, this section, (a). <sup>18</sup> McKean v. County of Northampton, 49 Pa. St. 519, 88 Am. Dec. 515; Dyer v. Osborne, 11 R. I. 321, 23 Am. Rep. 460; ante, §§ 289(c), 293(c).

<sup>19</sup> Saup v. Morgan, 108 Ill. 326. \*Thus, the situs of shares of stock, for the purpose of execution and attachment, is at the domicile of the corporation. See post, § 377.

And shares of stock in a domestic corporation, although owned by a nonresident, are property within the state, so that jurisdiction can be acquired by publication in a suit to establish title to the shares. Jellenik v. Huron Copper Mining Co., 177 U. S. 1, reversing 82 Fed. Abr. 108, 1 v. Second 57 Ind. 19 to the con 24 Bligh Co. 268, 1 Fed. Contra, Con., 177 U. S. 1, reversing 82 Fed. Conn. 567.

<sup>778.</sup> And see post, § 378(h), and cases cited in note 13, supra.

<sup>20</sup> Allen v. Pegram, 16 Iowa, 163; Mattingly v. Roach, 84 Cal. 207.

<sup>&</sup>lt;sup>21</sup> Manns v. Brookville Nat. Bank, 73 Ind. 243; and note 26, infra.

 <sup>&</sup>lt;sup>22</sup> Bradley v. Holdsworth, 3 Mees.
 & W. 422; Humble v. Mitchell, 11
 Adol. & E. 205, 1 Cum. Cas. 602;
 post, § 610.

<sup>&</sup>lt;sup>23</sup> Russell v. Temple, 3 Dane, Abr. 108, 1 Smith's Cas. 23; Weyer v. Second Nat. Bank of Franklin, 57 Ind. 198. See the early cases to the contrary in note 14, supra. <sup>24</sup> Bligh v. Brent, 2 Younge & C. 268, 1 Keener's Cas. 847.

Contra, Welles v. Cowles, 2 Conn. 567.

corporation owning land;25 that a mortgage or deed of trust of shares of stock is governed by the law relating to mortgages of personal property;26 that an action on a subscription to stock is not an action upon a contract for the sale of real estate, within a statute relating to the jurisdiction of courts.<sup>27</sup>

- (c) Shares of stock as "chattels" or as "goods, wares, and merchandises."—Although shares of stock are personal property,28 it has been held that they are not "chattels," or "goods and In England it is held that they are not "goods, wares, or merchandises," within the meaning of the seventeenth section of the statute of frauds.30 In this country, however, the contrary has been held in most of the states in which the question has arisen.31
- (d) Shares of stock as "choses in action," "credits," "money," or "securities."—Shares of stock in corporations are sometimes spoken of as "choses in action."32 They are somewhat in the nature of choses in action; but when we consider the rights of a shareholder and his relation to the corporation, it is clear that, strictly speaking, they are neither a chose in action nor a credit.<sup>33</sup>

<sup>26</sup> Tregear v. Etiwanda Water
Co., 76 Cal. 537, 9 Am. St. Rep.
245; Cates v. Baxter, 97 Tenn. 443. Compare Williamson v. New Jersey Southern R. Co., 26 N. J. Eq. 398.

27 York Park Building Ass'n v.

Barnes, 39 Neb. 834.

28 Supra, this section, (b). 29 Rex v. Copper, 5 Price, 217,

It has been held that the stock of a corporation is not goods and chattels, within the meaning of a statute regulating the mortgaging of goods and chattels, and requiring the filing of such a mortgage. Williamson v. New Jersey Southern R. Co., 26 N. J. Eq. 398. Compare cases in note 26. supra.

30 Humble v. Mitchell, 11 Adol. 10 Pa. St. 373. & E. 205, 1 Cum. Cas. 602.

31 Tisdale v. Harris, 20 Pick.

25 Baldwin v. Canfield, 26 Minn. zen v. Nicolay, 53 N. Y. 467; North v. Forest, 15 Conn. 400; post, § 610. 32 See Fisher v. Essex Bank, 5 Gray (Mass.) 373, 2 Keener's Cas. 1080, 1 Cum. Cas. 664; Warren v. Davenport Fire Ins. Co., 31 Iowa, 464, 1 Smith's Cas. 48; Wildman v. Wildman, 9 Ves. 174; Arnold v. Ruggles, 1 R. I. 165; People's Bank of Philadelphia v. Kurtz. 99 Pa. St. 344, 44 Am. Rep. 112; Denton v. Livingston, 9 Johns. (N. Y.) 96, 6 Am. Dec. 264; Union Bank of Tennessee v. State, 9 Yerg. (Tenn.) 490; Young v. South Tredegar Iron Co., 85 Tenn. 189, 4 Am. St. Rep. 752; Keyser v. Hitz, 2 Mackey (D. C.) 473; First Nat. Bank v. Smith, 65 III. 44; Vanstone v. Goodwin, 42 Mo. App. 39; Slaymaker v. Bank of Gettysburg,

33 Bridgman v. City of Keokuk, 72 Iowa, 42; Cates v. Baxter, 97 (Mass.) 9, 1 Cum. Cas. 604; Balt- Tenn. 443; New Orleans Nat. a late Iowa case it was held that they were not "credits," within the meaning of a statute allowing the deduction of debts from moneys and credits for the purposes of taxation. "Stock in corporations," said the court, "ordinarily \* \* \* credit, it is not an indebtedness to its owner, but, on the contrary, is an interest in the property of the corporation. Its owner holds an equitable interest in the property of the corporation, which is represented by the term 'stock,' and the extent of his interest is described by the term 'shares.' expression 'shares of stock,' when 'qualified by words indicating number and ownership, expresses the extent of the owner's interest in the corporation property. The interest is equitable, and does not give him the right of ownership to specific property of the corporation. But he does own the specific stock held in his name, and, under the rules of law, the property of the corporation is held by the corporation in trust for the stockholders. It will be readily seen that a share of stock is a thing owned by the stockholder. It is in no sense a debt owing to the stockholder. It is not, therefore, a credit."34

Shares of stock are clearly not "money." Nor are they "securities," or "securities for money."35

Banking Ass'n v. Wiltz, 4 Woods, by the defendant. Nightingal v. 43, 10 Fed. 330.

34 Bridgman v. City of Keokuk, 72 Iowa, 42.

35 Jones v. Brinley, 1 East, 1; Gosden v. Dotterill, 1 Mylne & K.

It has been held, therefore, that the receipt of stock is not the receipt of money, within the meaning of a contract to pay a certain estate "in money or securities" percentage on the receipt of any "money." East, 1.

ceived will not lie unless money bury, 10 Beav. 547). has been received, and it will not lie, therefore, for stock received in money or securities" does not

Devisme, 5 Burrows, 2589.

Shares of stock will not pass under a will bequeathing "money" (Gosden v. Dotterill, 1 Mylne & K. 56; Hotham v. Sutton, 15 Ves. & New Haven R. Co., 13 N. Y. 599, 434, 38 L. J. Ch. 692; Collins v. 627; Graydon v. Graydon, 23 N. J. Collins, L. R. 12 Eq. 455; Graydon Eq. 229; Atkins v. Gamble, 42 Cal. v. Graydon, 23 N. J. Eq. 229); nor under a will bequeathing all "securities for money" (Ogle v. Knipe, L. R. 8 Eq. 434, 38 L. J. Ch. 692); nor under a will bequeathing all (Graydon v. Graydon, 23 N. J. Eq. Jones v. Brinley, 1 229); nor under a will bequeath-ing all property "invested in bonds An action for money had and re- or securities" (Hudleston v. Goulds-

An exception in a will of "estate

(e) Title to shares as between husband and wife.—Shares of stock, although they are personal property, and although they cannot be regarded as choses in action in the proper sense, are so much in the nature of choses in action that they are not property in possession, when owned by a married woman, so as to vest in the husband at common law without being reduced to his possession. On the contrary, they are subject to the same rules as choses in action. If reduced to his possession by the husband in the lifetime of the wife, they belong to him, but, if not reduced to possession in the lifetime of the wife, they survive to her on the death of the husband, or pass to her administrator on her death.36

## § 377. Liability of shares of stock to execution, attachment, garnishment, etc.

At common law, a chose in action, being intangible and incapable of manual seizure and delivery, cannot be taken on execution; and shares of stock in a corporation, which are in the nature of choses in action, are subject to the same rule. They are not subject to execution for the debts of the holder, unless they are made so by statute.37 Nor can they be seized under the statutes relating to attachment, unless the statute so

373; Arnold v. Ruggles, 1 R. I. 165; Wilder v. Aldrich, 2 R. I. 518; Winslow v. Crocker, 17 Me. 29; Stanwood v. Stanwood, 17 Mass. 57; Wells v. Tyler, 25 N. H. 340; 57; Wells v. Tyler, 25 N. H. 340; This is true, even though the Rice v. McReynolds, 8 Lea (Tenn.) charter of a corporation may ex-

C.) 195; Blair v. Compton, 33 Mich. 236.

include shares of stock. Graydon 414; Van Norman v. Jackson Counv. Graydon, 23 N. J. Eq. 229. ty Circuit Judge, 45 Mich. 204; 36 Wildman v. Wildman, 9 Ves. Denton v. Livingston, 9 Johns. (N. 174, 177; Nicholson v. Drury Build- Y.) 96, 6 Am. Dec. 264; Foster v. lings Estate Co., 7 Ch. Div. 48, 55; Potter, 37 Mo. 525; Robinson v. Blake v. Jones, Bailey Eq. (S. C.) Spaulding Gold & Silver Min. 141, 21 Am. Dec. 530; Slaymaker Co., 72 Cal. 32; Coombs v. Jordan, v. Bank of Gettysburg, 10 Pa. St. 3 Bland Ch. (Md.) 284, 22 Am. Dec. 236; Barnes v. Hall, 55 Vt. 420; Wells v. Price (Idaho) 56 Pac. 266. Compare Colt v. Ives, 31 Conn. 25. 81 Am. Dec. 161.

36; In re Reciprocity Bank, 22 N. pressly declare that its shares, for Y. 9, 15. 37 Howe v. Starkweather, 17 real estate. Cooper v. Swamp Mass. 240; Slaymaker v. Bank of Canal Co., 2 Murph. (N. C.) 195. Gettysburg, 10 Pa. St. 373; Cooper And see Coombs v. Jordan, 3 v. Swamp Canal Co., 2 Murph. (N. Bland Ch. (Md.) 284, 22 Am. Dec.

provides in express terms or by necessary implication.<sup>38</sup> in the absence of statutory provision, can they be seized and sold on a tax warrant, 39 or attachment for taxes. 40

Statutory authority.—Although shares of stock in corporations cannot be reached and subjected to the holder's debts by execution or attachment, unless such a remedy is provided by statute, it is perfectly competent for the legislatures to enact such statutes, and they have been enacted in most jurisdictions.41 When a statute makes all "personal property" subject to execution or attachment, and declares shares of stock to be personal property, or, it would seem, even without an express declaration to the latter effect, 42 it renders shares of stock subject. 43 In construing such a statute, however, and in construing other statutes using general terms, the courts have differed. Some of the decisions are given in the note below.44

592, 1 Keener's Cas. 855; Foster v. Potter, 37 Mo. 525; Kennedy v. Mary Lee Coal & Ry. Co., 93 Ala. 494; Armour Bros. Banking Co. v. St. Louis Nat. Bank, 113 Mo. 12, 35 Am. St. Rep. 691; Merchants' Mutual Ins. Co. v. Brower, 38 Tex. 230; Sowles v. National Union Bank, 82 Fed. 696; Wells v. Price (Idaho) 56 Pac. 266.

39 Barnes v. Hall, 55 Vt. 420.

40 Kennedy v. Mary Lee Coal &

Ry. Co., 93 Ala. 494.

41 Titcomb v. Union Marine & Fire Ins. Co., 8 Mass. 326; Blair v. Compton, 33 Mich. 414; People v. Goss & Phillips Mfg. Co., 99 III. 355: Oldacre v. Butler, 116 Ala. 652.

Under the New York attachment law, shares of stock may be reached and subjected in supplementary proceedings. O'Brien v. Mechanics' & Traders' Fire Ins. Co., 56 N. Y. 52; Barnes v. Morgan, 3 Hun (N. Y.) 703.

It seems that shares in a national bank may be taken under in Illinois that shares were subexecution or attachment under a ject to attachment where the statstate statute to the same extent ute allowed execution of the writ

38 Plimpton v. Bigelow, 93 N. Y. of any legislation by congress to Oldacre v. Butler, 116 prevent.

> Contra, Sowles v. National Union Bank of Swanton, 82 Fed. 696.

When shares of stock are attached, the attachment will cover dividends thereon. Jacobus Monongahela Nat. Bank of Brownsville, 35 Fed. 395. See, also, Moore v. Gennett, 2 Tenn. Ch. 375.

42 Ante, § 376(b).

48 See Brock v. Ruttan, 1 Upper Can. C. P. 218; Union Nat. Bank of Chicago v. Byram, 131 Ill. 92. 44 It was held in Georgia that

shares of stock were not subject to attachment under a statute allowing attachment of "the estate both real and personal" of the debtor. Haley v. Reid, 16 Ga. 437.

And in Missouri it was held that shares were not subject to attachment under a statute allowing attachment of "real and personal property." Foster v. Potter, 37 Mo. 525.

On the other hand, it was held as any other shares, in the absence "upon the lands, tenements, goods,

The nature of a particular corporation may be such that its shares do not come within the general laws allowing shares of stock to be seized and sold on execution or attachment. has been held, for example, that stock issued by an association organized under a statute for "yachting, hunting, fishing, boating, rowing, and other lawful sporting purposes," was not subject to levy and sale under a statute authorizing sale on execution of the share or interest of a stockholder in any bank, insurance company, or any other joint-stock company, incorporated under the laws of the state.45

Garnishment or trustee process.—Garnishment, or, as it is called in some jurisdictions, trustee process, is generally an appropriate remedy only in cases in which there is a debt due from the garnishee to the debtor, and since there is no debt (except as to dividends declared) between a corporation and its shareholders by reason of their ownership of stock, garnishment or trustee process is not a proper remedy by which to subject shares of stock to the satisfaction of a debt of the owner, unless it is made so by statute.46 In a number of states, however, shares of stock are expressly made subject to garnishment, or, if not made so in express terms, the provisions relating to execu-

fects of the debtor," as the words "rights" and "effects" were broad enough to include shares of stock. Union Nat. Bank of Chicago v. Byram, 131 Ill. 92.

In New Jersey it was held that

The New York statute (Code Civ. Proc. § 649, subd. 3) requiring, on an attachment of stock, a certified copy of the warrant, and a notice showing the property attached, to Mobile v. Leavens, 4 Ala. 753; be left with the president or head of the corporation, or the secretary, cashier, or managing agent thereof, mour Bros. Banking Co. v. St. has been held to apply only to Louis Nat. Bank, 113 Mo. 12, 35 stock in domestic corporations. stock in domestic corporations. Am. St. Rep. 691.

chattels, rights, moneys and ef- Simpson v. Jersey City Contracting

Co., 61 N. Y. Supp. 1033.

45 Lyon v. Denison, 80 Mich. 371. It was held that the Tennessee statute making the stock of all private corporations thereafter created by "special law" subject to shares of stock could be attached of any private corporation, and apunder a statute allowing attachment of "rights and credits." Curbination of the control execution referred to the creation der a general law, as required by the constitution. Nashville Trust Co. v. Weaver, 102 Tenn. 66.

46 Ross v. Ross, 25 Ga. 297; Planters' & Merchants' Bank of

tion, attachment, and garnishment are construed as impliedly making them so.47

Mode of levy and sale.—In levying upon and selling shares of stock on execution, attachment, or garnishment, in pursuance of a statute, the provisions of the statute as to the mode of levy and sale must be substantially complied with, or the sale will be absolutely void.48 Thus, if the statute so requires, notice must be properly given to the stockholder or the corporation, or to both;49 the number of shares must be ascertained and stated;50

47 Old Second Nat. Bank of Bay Hencke, 99 Wis. 660; O. L. Packard City v. Williams, 112 Mich. 564; Chesapeake & Ohio R. Co. v. Paine, 29 Grat. (Va.) 502; Harrell v. Mexico Cattle Co., 73 Tex. 612; Smith v. Traders' Nat. Bank, 74 Tex. 457; Younkin v. Collier, 47 Fed. 571; Edwards v. Beugnot, 7 Cal. 162; Puget Sound Nat. Bank of Everett v. Mather, 60 Minn. 362. And see Banning v. Sibley, 3 Minn. 389, 405.

Stock is subject to garnishment in Michigan under statutes providing that stock may be taken on execution, and providing for charging a garnishee with property, money, or effects in his hands. Old Second Nat. Bank of Bay City v. Williams, 112 Mich. 564.

The Wisconsin statute enabling a creditor to reach property of his debtor in the possession or control of a third person by garnishment does not enable him to reach shares of stock owned by his debtor by garnishment of the person in possession of the certificates of the stock. O. L. Packard Machinery Co. v. Laev, 100 Wis. 644.

48 Deutschman v. Byrne, 64 Ark. 111; Titcomb v. Union Marine & Fire Ins. Co., 8 Mass. 326; Howe v. Starkweather, 17 Mass. 240; Blair v. Compton, 33 Mich. 414; Princeton Bank v. Crozer, 22 N. J. Law, 383, 53 Am. Dec. 254; Stamford Bank v. Ferris, 17 Conn. 259; Younkin v. Collier, 47 Fed. 571; A levy upon and Abbot v. Kimball, 68 N. H. 303; shares of stock ow Feige v. Burt, 118 Mich. 243, 74 ing to" the debtor Am. St. Rep. 390; Barthell v. cases above cited.

Machinery Co. v. Laev, 100 Wis. 644; Wells v. Price (Idaho) 56 Pac. 266.

As to sales of shares in a block, instead of in parcels, see Morris v. Connecticut & Passumpsic Rivers R. Co., L. R. 2 Q. B. (Montreal) 303; Connecticut & Passumpsic Rivers R. Co. v. Morris, 14 Can. Sup. Ct. 318.

That a sale of shares on execution at nine o'clock at night, when there are few persons present, is void, see McNaughton v. McLean. 73 Mich. 250.

That a bond given to procure an attachment of shares will not be increased because the value of the shares may decrease, and that such a decrease does not render the sureties liable, see Miller v. Ferry, 50 Hun (N. Y.) 256. 49 Commercial Nat. Bank v.

Farmers' & Traders' Nat. Bank, 82 Iowa, 192; Moore v. Marshalltown Opera-House Co., 81 Iowa, 45; Deutschman v. Byrne, 64 Ark. 111; Princeton Bank v. Crozer, 22 N. J. Law, 383, 53 Am. Dec. 254; Voorhis v. Terhune, 50 N. J. Law, 147, 7 Am. St. Rep. 781.

50 Blair v. Compton, 33 Mich. 414; Keating v. J. Stone & Sons Live-Stock Co., 83 Tex. 467, 29 Am. St. Rep. 670; People v. Goss & Phillips Mfg. Co., 99 Ill. 355.

A levy upon and sale of "all the shares of stock owned and belong-ing to" the debtor is void. See the

the sale must be properly advertised;<sup>51</sup> a copy of the writ must be left with the corporation, properly indorsed.<sup>52</sup>

If the charter of a corporation fixes the right to take shares of its stock on execution or attachment, or the mode of levying upon and selling the same, it supersedes a general law on the subject previously enacted; but it is otherwise where the general law is subsequently enacted.53

The corporation, and not the holder of the certificates of stock, is the proper party upon whom to serve attachment or garnishee process to reach and subject shares of stock.54

Title.—Of course shares of stock cannot be attached or taken on execution if they do not belong to the debtor, as where he has transferred them in good faith and for value, or holds them merely as trustee or pledgee; and generally it can make no difference that he appears on the books of the corporation as owner.55 Levy of an execution or attachment upon shares of stock takes precedence over a sale of the stock previously negotiated, but not consummated by an actual transfer and delivery of the certificates of stock until after the levy, although the transfer and delivery of the certificates may have been without notice of the attachment.56

rine & Fire Ins. Co., 8 Mass. 326.

Starkweather, 17 Mass. 240.

54 Younkin v. Collier, 47 Fed. 571. 453; Beckwith v. Burrough, 13 R.

I. 294; Lippitt v. American Wood Paper Co., 15 R. I. 141, 2 Am. St. Rep. 886, 2 Keener's Cas. 1095. See, also, Hitchcock v. Galveston Wharf Co., 50 Fed. 263.

See, however, Tufts v. Volken-

ing. 122 Mo. 631.

Under a Michigan statute authorizing the levy of execution on shares of stock, and requiring the officer in charge of the records of the company to give a certificate of 752.

51 Howe v. Starkweather, 17 the number of shares held by the Mass. 240; Titcomb v. Union Ma- debtor, it was held that shares owned by the debtor, but standing in 52 Stamford Bank v. Ferris, 17 the name of a third person on the books of the company, were not 53 Titcomb v. Union Marine & subject to levy on execution. Fire Ins. Co., 8 Mass. 326; Howe v. Feige v. Burt, 118 Mich. 243, 74 Am. St. Rep. 390.

Stock held by a debtor as treas-55 Mowry v. Hawkins, 57 Conn. urer, or as trustee, is not subject to levy under an execution running against him individually. ville Trust Co. v. Weaver, 102

Tenn. 66.

As to the agent's or trustee's liability to the principal or cestui que trust, where stock has been seized and sold for the former's debt, see Hovey v. Bradbury, 112 Cal: 620.

56 Young v. South Tredegar Iron Co., 85 Tenn. 189, 4 Am. St. Rep. The rights of an unregistered owner of shares of stock, as against an execution or attachment by a creditor of the person appearing upon the books of the corporation as owner, is considered in treating of the transfer of shares and registration of transfers in a subsequent chapter.<sup>57</sup>

Equitable title or interest.—Ordinarily, it is only the legal interest in property which can be reached by an execution or attachment, and shares of stock cannot be taken under execution or attachment by a creditor of one who has merely an equitable title or interest.<sup>58</sup> In some jurisdictions, however, the statutes are broad enough to obviate this difficulty.<sup>59</sup> In some, but not all, jurisdictions, the statutes are broad enough, as where they allow equitable as well as legal interests and rights to be levied upon, to permit a creditor to levy an execution or attachment upon shares of stock which have been fraudulently transferred by the debtor, instead of first suing in equity to set the transfer aside.<sup>60</sup>

Ordinarily, a mortgage or pledge of shares of stock does not prevent a creditor of the mortgagor or pledgor from levying thereon, and subjecting the equity of redemption, as in the case of other property.<sup>61</sup>

Situs of shares for purpose of execution or attachment—Jurisdiction.—Although, for the purposes of taxation, as we have seen

57 Post, § 590.

58 Gypsum, Plaster & Stucco Co. v. Grove, 97 Mich. 631; Van Norman v. Circuit Judge for Jackson County, 45 Mich. 204; Nabring v. Bank of Mobile, 58 Ala. 204; Lippitt v. American Wood Paper Co., 15 R. I. 141; 2 Am. St. Rep. 886, 2 Keener's Cas. 1095.

59 See the cases cited in the notes following.

60 Beckwith v. Burrough, 14 R. I. 366, 51 Am. Rep. 392; Scott v. Indianapolis Wagon Works, 48 Ind. 75; Curtis v. Steever, 36 N. J. Law, 304; National Bank of New London v. Lake Shore & Michigan Southern Ry. Co., 21 Ohio St. 221.

But see Van Norman v. Circuit Judge for Jackson County, 45 Mich.

61 Norton v. Norton, 43 Ohio St. 509; Middletown Savings Bank v. Jarvis, 33 Conn. 372; Manns v. Brookville Nat. Bank, 73 Ind. 243; Vantine v. Morse, 104 Mass. 275; Foster v. Potter, 37 Mo. 525; Edwards v. Beugnot, 7 Cal. 162; Simpson v. Jersey City Contracting Co., 61 N. Y. Supp. 1033.

But see, to the contrary, Nabring v. Bank of Mobile, 58° Ala. 204. And compare Lippitt v. American Wood Paper Co., 15 R. I. 141, 2 Am. St. Rep. 886, 2 Keener's Cas. 1095 in another chapter, 62 and for some other purposes, shares of stock follow the domicile of the owner, like other personal property, unless otherwise provided by statute, their situs for the purpose of execution or attachment is held to be in the state where the corporation resides, that is, the state by or under the laws of which the corporation was created, and it has been held, therefore, that they cannot be levied upon in another state, and that it makes no difference that the debtor resides there, or that the certificates of the stock are found there. 63

In a New York case it was said, speaking of a statute allowing the attachment of shares of stock: Such a statute "has an appropriate application to shares in domestic corporations. Such corporations are completely subject to the jurisdiction of

62 Ante, § 289(c).

63 Winslow v. Fletcher, 53 Conn. 390, 55 Am. Rep. 122; Ireland v. Globe Milling & Reduction Co., 19 R. I. 180, 61 Am. St. Rep. 756, where it was held that the situs of corporate stock, for the purposes of execution and attachment, is the domicile of the corporation, and that place only, which is within the state creating it; that a stat-ute which authorizes "the attachment of the shares of the defendant in any corporation," etc., is to be construed in view of the fundamental principle that property is not subject to attachment unless it is actually or constructively within the jurisdiction of the court issuing the attachment, and, therefore, that shares of stock in a foreign corporation owned by a nonresident defendant could not be reached by attachment in Rhode Island, although the officers of the corporation were within the state, and its business was being carried on there.

See, also, Plimpton v. Bigelow, attachment in Ten 93 N. Y. 592, 1 Keener's Cas. 855; the debtor and own Smith v. Downey, 8 Ind. App. 179; is a nonresident, Christmas v. Biddle, 13 Pa. St. 223; cates of stock are Armour Bros. Banking Co. v. St. sion beyond the lin Louis Nat. Bank, 113 Mo. 12, 35 Compare, however, Am. St. Rep. 691; Pinney v. Necited in this note.

vills, 86 Fed. 97; Morton v. Grafflin, 68 Md. 545; Reid Ice Cream Co. v. Stephens, 62 Ill. App. 334; Moore v. Gennett, 2 Tenn. Ch. 375; New Jersey Sheep & Wool Co. v. Traders' Deposit Bank (Ky.) 46 S. W. 677.

There are some decisions in conflict with those above cited, and holding shares in a foreign corporation subject to attachment or garnishment. See Puget Sound Nat. Bank of Everett v. Mather, 60 Minn. 362; Young v. South Tredegar Iron Co., 85 Tenn. 189, 4 Am. St. Rep. 752.

It was held, in Young v. South Tredegar Iron Co., 85 Tenn. 189, 4 Am. St. Rep. 752, that since, under the statutes of Tennessee, a foreign corporation becomes a domestic corporation of that state upon complying with the statutes for the purpose of doing business there, shares of stock in such a corporation, which has complied with such statutes, are subject to attachment in Tennessee, although the debtor and owner of the shares is a nonresident, and the certificates of stock are in his possession beyond the limits of the state. Compare, however, the other cases our courts, and may be compelled to recognize a title to corporate shares derived under proceedings by attachment. In respect to foreign corporations such power does not exist, and it could scarcely be expected that the courts of another state would recognize a title to corporate stock in one of its own corporations, founded upon a sale under an attachment issued by our courts against a nonresident, when the only semblance of jurisdiction over the property was the service of notice in the attachment proceedings, upon an officer or agent of the corporations The abstract entity—the corporation—is the owner and only owner of the property. We do not doubt that shares for the purpose of attachment proceedings may be deemed to be in the possession of the corporation which issued them, but only at the place where the corporation by intendment of law always remains, to wit, in the state or country of its creation. In all other places it is an alien. It may send its agents abroad or transact business abroad as any other inhabitant may do, without passing personally into the foreign jurisdiction or changing its legal residence."64

In a Connecticut case it was said of certificates of stock in a foreign corporation: "A share of stock in a corporation consists of a set of rights and duties between the corporation and the owner of the share. These rights and duties are in fact and law quite distinguishable from the certificates and the power to transfer those rights and duties. The certificate is evidence that the person therein named possesses those rights and is subject to those duties, but is not in law the equivalent of those rights and duties. They are muniments of title, but not the title itself; much less the real property. While these certificates are in themselves valuable for some purposes, and to some extent may properly be regarded as property, yet they are distinct from the holder's interest in the capital stock of the corporation, and are not goods and effects within the meaning of the statute relating to foreign attachment. They are no

<sup>64</sup> Plimpton v. Bigelow, 93 N. Y. 592, 1 Keener's Cas. 855.

more subject to an attachment or a trustee process than a The debt is subject to attachment, but the promissory note. note itself, which is simply evidence of the debt, is not. with stock. That may be attached, but the certificates cannot be. \*\*65

Of course, stock owned by a nonresident debtor in a domestic corporation may be attached where the statutes allow, as they generally do, attachment of the property of a nonresident, and make shares of stock subject to attachment; and it can make no difference that the certificates of stock are not within the jurisdiction of the court.66

Equity jurisdiction to reach and subject shares to payment of debts.—A court of equity has undoubted jurisdiction to set aside a transfer of choses in action or shares of stock fraudulently made by the owner with intent to hinder, delay, and defraud creditors, and to direct a sale of the same, and apply the proceeds to the payment of his debts, unless the creditor has an adequate and complete remedy at law; or it may reach and subject to the payment of debts money or property which the debtor has fraudulently invested in choses in action or shares of stock for the purpose of putting it beyond the reach of an execution.<sup>67</sup> By the weight of authority, however, a court of equity has no jurisdiction to subject shares of stock to the payment of debts

<sup>390, 55</sup> Am. Rep. 122. See, also, Armour Bros. Banking Co. v. St. Louis Nat. Bank, 113 Mo. 12, 35 Nevills, 86 Fed. 97.

Co., 85 Tenn. 189, 4 Am. St. Rep. Ry. Co., 21 Ohio St. 221; and other

<sup>67</sup> Donovan v. Finn, 1 Hopk. Ch. 236.

<sup>65</sup> Winslow v. Fletcher, 53 Conn. (N. Y.) 59, 14 Am. Dec. 531; Colbert v. Sutton, 5 Del. Ch. 294; Van Norman v. Circuit Judge for Jack-Louis Nat. Bank, 113 Mo. 12, 35 son County, 45 Mich. 204; Gillett Am. St. Rep. 691; Christmas v. v. Bate, 86 N. Y. 87; Spader v. Biddle, 13 Pa. St. 223; Pinney v. Hadden, 5 Johns. Ch. (N. Y.) 280, affirmed in Hadden v. Spader, 20 66 Young v. South Tredegar Iron Johns. (N. Y.) 554, 562; State Bank of Syracuse v. Gill, 23 Hun 752; Chesapeake & Ohio R. Co. v. (N. Y.) 410; Bayard v. Hoffman. Paine, 29 Grat. (Va.) 502; Na 4 Johns. Ch. (N. Y.) 450; Skowtional Bank of New London v. hegan Bank v. Cutler, 49 Me. 315; Lake Shore & Michigan Southern Scott v. Indianapolis Wagon Works, Ry. Co., 21 Ohio St. 221; and other 48 Ind. 75; Lathrop v. McBurney, cases cited in the notes preced-71 Ga. 815; Coombs v. Jordan, 3 ing. Bland Ch. (Md.) 284, 22 Am. Dec.

merely because they are not subject to execution or attachment, 68 unless it is otherwise provided by statute. 69

"According to our distribution of jurisdictions, suits for the recovery of ordinary debts are appropriated to the courts of common law; and the proceedings for enforcing the judgments rendered in such suits are alike allotted to those courts. any such case, where the subject of the suit is exclusively of legal cognizance, a court of equity has no jurisdiction to enforce the judgment by its own methods of proceeding, or to give a better remedy than the law gives. If the remedies of the law are imperfect, equity, as has been often said in the English chancery, has no jurisdiction to give execution in aid of the infirmity of the law. When any fact giving equitable jurisdiction intervenes in the transactions between creditor and debtor, such a fact becomes a foundation of relief in this court; but in any ordinary case free from fraud or injustice, the execution of the judgment, and the methods of compelling satisfaction are confined to the courts of law. When a creditor comes to this court for relief, he must come not merely to obtain judgment or satisfaction of a judgment, but he must present facts which form a case of equitable jurisdiction. He must show that the debtor has made some fraudulent disposition of his property, or that the case stands infected with some trust, collusion, or injustice, against which it is the province of this court to give relief. In such cases this court has jurisdiction, not for the purpose of giving a species of execution which the courts of law do not afford, but for the purpose of giving relief in the particular cases allotted to its jurisdiction; and when the cause, by reason of such facts, is properly here, the court proceeds

<sup>68</sup> Dundas v. Dutens, 1 Ves. Jr. v. Waddell, 2 Sandf. Ch. (N. Y.) 196; Bank of England v. Lunn, 15 495. Ves. 569; Donovan v. Finn, 1 Hopk. Ch. (N. Y.) 59, 14 Am. Dec. 531; Erwin v. Oldham, 6 Yerg. (Tenn.) 185, 27 Am. Dec. 458; Disborough v. Outcalt, 1 N. J. Eq. 298; Williams v. Reynolds, 7 Ind. 622. The contrary was held in Storm (Tenn.) 196.

See, also, Watkins v. Dorsett, 1 Bland Ch. (Md.) 530; Coombs v. Jordan, 3 Bland Ch. (Md.) 284, 22 Am. Dec. 236.

<sup>69</sup> Brightwell v. Mallory, 10 Yerg.

upon all the circumstances of the case to give final and equitable relief."70

#### § 378. Certificates of stock.

(a) Nature of certificate in general.—It is usual for a corporation having a capital stock divided into shares to issue to its stockholders a certificate of stock or stock certificates, certifying or showing that the person named therein is the owner of the number of shares therein specified. It may also state the terms, or some of the terms, of the holder's contract with the corporation, the character of the stock, whether it is full-paid and nonassessable, the manner in which it must be transferred, whether it is transferable at all, etc.

It is well settled that a certificate of stock in a corporation is not the stock itself. It is the mere evidence of the holder's ownership of the stock and of his rights as a stockholder to the extent specified therein, just as a promissory note is merely the evidence of the debt secured thereby, and as title deeds are merely the evidence of the ownership of land.71 "A share of stock in a corporation consists of a set of rights and duties between the corporation and the owner of the share. These rights and duties are in fact and law quite distinguishable from the certificates and the power to transfer those rights and duties. The certificate is evidence that the person therein named possesses those rights and is subject to those duties, but is not in law the equivalent of those rights and duties. They are muniments of title, but not the title itself; much less the real property."72

<sup>(</sup>N. Y.) 59, 14 Am. Dec. 531.

<sup>71</sup> Winslow v. Fletcher, 53 Conn. 390, 55 Am. Rep. 122; Christmas v. Biddle, 13 Pa. St. 223; Cartwright v. Dickinson, 88 Tenn. 476, 17 Am. Webb v. Baltimore & Eastern Shore v. Laev, 100 Wis. 644.

<sup>70</sup> Donovan v. Finn, 1 Hopk. Ch. R. Co., 77 Md. 92, 39 Am. St. Rep.

<sup>72</sup> Winslow v. Fletcher, 53 Conn.

<sup>390, 55</sup> Am. Rep. 122. In a late Wisconsin case it was said: "Corporate stock is proper-St. Rep. 910; Armour Bros. Bank-ty, but the certificate of such stocking Co. v. St. Louis Nat. Bank, 113 is not the stock. It is much like Mo. 12, 35 Am. St. Rep. 691; Burr a title deed or a bill of sale, which v. Wilcox, 22 N. Y. 551; California is not the property itself, but sim-Southern Hotel Co. v. Callender, ply the evidence of title to proper-94 Cal. 120, 28 Am. St. Rep. 99; ty." O. L. Packard Machinery Co.

(b) Necessity for issue of certificates.—From the fact that a certificate of stock is not the stock itself, but merely evidence of the stockholder's rights, it follows that, in the absence of provision to the contrary, the issue of certificates of stock is not at all necessary, either to the existence of a joint-stock corporation, or to make one a stockholder in such a corporation, for one may be a stockholder without the formal written evidence of his rights. In the absence of provision or agreement to the contrary, therefore, a subscriber for stock in a corporation, or, except as hereafter stated, a purchaser of stock, becomes a stockholder as soon as his subscription is accepted by the corporation, and statutory or charter conditions are performed or fulfilled, or as soon as the purchase is completed, as the case may be, whether any certificate of stock is issued to him or not; and as soon as he thus becomes a stockholder, although he may have no certificate, he is entitled to all the rights of a stockholder, including the right to dividends and the right to vote, etc., and is subject to all the liabilities of a stockholder, including liability to an action on his subscription, and liability to creditors in case of the corporation's insolvency.<sup>73</sup> It can make no difference in this respect

78 Chester Glass Co. v. Dewey, 16 Mass. 94, 8 Am. Dec. 128; Spear v. Crawford, 14 Wend. (N. Y.) 20, 28 Am. Dec. 513; Burr v. Wilcox, 22 N. Y. 551; Rutter v. Kilpatrick, 63 N. Y. 604; Wheeler v. Millar, 90 N. Y. 353; Kohlmetz v. Calkins, 16 App. Div. (N. Y.) 518; New Albany & Salem R. Co. v. McCormick, 10 Ind. 499, 71 Am. Dec. 337; Heaston v. Cincinnati & Ft. Wayne R. Co., 16 Ind. 275, 79 Am. Dec. 430; Miller v. Wild Cat Gravel Road Co., 52 Ind. 51; Beckett v. Houston, 32 Ind. 393; Chandler v. Northern Cross R. Co., 18 Ill. 190; Wemple v. St. Louis, Jerseyville & S. R. Co., 120 Ill, 196; Columbia Electric

480; Schaeffer v. Missouri Home Ins. Co., 46 Mo. 248; Webb v. Baltimore & Eastern Shore R. Co., 77 Md. 92, 39 Am. St. Rep. 396; Chaffin v. Cummings, 37 Me. 76; Barron v. Burrill, 86 Me. 66; Cartwright v. Dickinson, 88 Tenn. 476, 17 Am. St. Rep. 910; Paducah & Memphis R. Co. v. Parks, 86 Tenn. 554; Frenkel v. Hudson, 82 Ala. 158, 60 Am. Rep. 736; California Southern Hotel Co. v. Callender, 94 Cal. 120, 28 Am. St. Rep. 99; San Joaquin Land & Water Co. v. Beecher, 101 Cal. 70; Pacific Fruit Co. v. Coon, 107 Cal. 447; Astoria & South Coast Ry. Co. v. Hill, 20 Or. 177; Nebraska Exposition Ass'n Co. v. Dixon, 46 Minn. 463; Marson v. Townley, 46 Neb. 893; Waukon son v. Diether, 49 Minn. 423; Walter A. Woods Harvester Co. v. Robbins, 56 Minn. 48; Holland v. DuBrunswick R. Co., 44 Ga. 597; luth Iron Mining & Development Co., 65 Minn. 324, 60 Am. St. Rep. Ayres, 56 Ga. 230; Crumlish v. that the charter of the corporation, or the general law under which it is formed, expressly declares that the stock shall be divided into shares, and that certificates shall be issued to shareholders, for it is not intended by such a provision to make the certificates necessary.<sup>74</sup> Of course, if a subscription for stock expressly requires that a certificate shall be issued as a condition precedent to liability, this is one of the terms or conditions of the subscriber's contract, and its issue or tender is necessary before the corporation can maintain an action on the subscription, unless the condition is waived.75

This rule does not apply where a person or corporation sells shares of stock. In such a case the issue or tender of a certificate as evidence of the stock is a condition precedent to the right to maintain an action for the price.76

(c) Certificate of stock as property.—A certificate of stock, that is, the certificate itself, as distinguished from the stock which it represents, is undoubtedly property. If it is wrongfully detained from the true owner, or wrongfully converted by another, it may be recovered in an action of detinue or replevin, or its value may be recovered in an action of trover.77

Shenandoah Valley R. Co., 40 W. ganization, in exchange for prop-Va. 627; Kerchner v. Gettys, 18 S. C. 521; Glenn v. Rosborough, 48 by entering the stock on the books S. C. 272; McComb v. Barcelona Apartment Ass'n, 134 N. Y. 598, affirming 56 Hun, 644; Biscoe v. Tucker, 11 Ark. 145; Pendery v. Carleton (C. C. A.) 87 Fed. 41; Watter A. Wood Harvester Co. v. Jefferson, 71 Minn. 367.

One who executes notes in pay

One who executes notes in payment for stock is a stockholder, although no certificate of stock is issued. Glenn v. Rosborough, 48

S. C. 272.

When land is conveyed to a corporation by a stockholder in payment of his subscription, the company is a purchaser for valuable consideration, whether certificates of stock are issued to him or not. Frenkel v. Hudson, 82 Ala. 158, 60 Am. Rep. 736.

An agreement to give stock in a 135. proposed corporation, upon its or-

75 Marson v. Deither, 49 Minn. 423; Courtright v. Deeds, 37 Iowa,

76 Marson v. Deither, 49 Minn. 423; Walter A. Wood Harvester Co. v. Jefferson, 71 Minn. 367; Kohlmetz v. Calkins, 16 App. Div. (N. Y.) 518; Considerant v. Brisbane, 14 How. Pr. (N. Y.) 487; St. Paul, Stillwater & T. F. R. Co. v. Robbins, 23 Minn. 439; Summers v. Sleeth, 45 Ind. 598; Clark v. Continental Improvement Co., 57 Ind.

77 Neiler v. Kelley, 69 Pa. St.

- (d) Certificate of stock as a chose in action, etc.—A certificate of stock is in the nature of a chose in action, or, rather, of an instrument evidencing a chose in action, but, properly speaking, it is not a chose in action. Nor is it a credit, or money, or a security.<sup>78</sup>
- (e) Certificate of stock as a negotiable instrument.—As we shall see more at length in a subsequent chapter, shares of stock are transferable by assignment or transfer of the certificate; but the certificate is not a negotiable instrument, and the assignee or transferee, in the absence of elements of estoppel, acquires no title if the assignor or transferrer had no title, and he takes it, in the absence of elements of estoppel, subject to equities existing against the assignor or transferrer. A certificate of stock, however, is regarded as so far negotiable that a transferee for value and in good faith takes a title to the stock free from latent equities between prior parties in the line of transmission, and he may acquire a good title, even when his transferrer had no title, if there are elements of estoppel.
- (f) Issue of certificate as a transfer of stock.—The issue of a new certificate of stock to a transferee of shares is one of the formalities in transferring stock, as we shall see in a subsequent chapter. But the issue of a certificate to original subscribers for stock is not in any sense a transfer of stock. Therefore it is not within a provision of the charter or by-laws that stock shall be transferable only on the books of the company. "The issuing of the original certificates," said Judge Selden in a New York case, "is in no sense a transfer of stock. The interest of

403; Williams v. Archer, 5 C. B. 318; Williams v. Reel River Land & Mineral Co., 55 Law T. (N. S.) 689; Daggett v. Davis, 53 Mich. 35, 51 Am. Rep. 91. See Merritt v. American Steel-Barge Co., 24 C. C. A. 530, 79 Fed. 228, as to which see infra, this section, (h). But replevin will not lie to recover the shares of stock. Ante, \$376(a).

78 See ante, § 376(d), and cases there cited.

79 Young v. South Tredegar Iron Co., 85 Tenn. 189, 4 Am. St. Rep. 752; East Birmingham Land Co. v. Dennis, 85 Ala. 565, 7 Am. St. Rep. 73.

See post,  $\S\S$  571, 594, and cases there cited.

80 Knox v. Eden Musee American Co., 148 N. Y. 441, 51 Am. St. Rep. 700, 2 Kener's Cas. 1121,

See post, §§ 571(c), 595.

the parties to whom they are issued is the same before as after such issue. The certificate is simply a written acknowledgment by the company of the interest of the subscribers in its property and franchises. It transfers nothing from the company to the subscriber, but simply affords to the latter evidence of his right."<sup>81</sup>

- (g) Transfer of certificate as a transfer of the stock.—While a certificate of stock is not the stock itself, it represents the stock for some purposes,—as evidence of the holder's rights, and for the purpose of transfer. The stock itself, being intangible, is not capable of manual delivery, and it is generally transferred or pledged by transfer or pledge of the certificate. The transfer of the certificate is a "symbolical" delivery of the stock.<sup>82</sup>
- (h) Jurisdiction over certificate as jurisdiction over stock.—A court can exercise jurisdiction over a certificate of stock—that is, over the certificate itself, as distinguished from the stock it represents—if the certificate is within its jurisdiction. ample, there can be no doubt that replevin will lie to recover possession of a certificate of stock, if the certificate is within the jurisdiction of the court, although the corporation may be in another state, so that the situs of the shares of stock is in the other state. In the nature of things, however, since a certificate of stock is not the stock itself, but mere evidence of the stockholder's interest in the corporation,a distinction which is thoroughly well-settled,83—jurisdiction over a certificate of stock can confer no jurisdiction over the stock itself, where the stock is not within the jurisdiction of the The situs of shares of stock is at the residence of the corporation, and does not follow the certificate. As we have seen, the situs of shares of stock for the purpose of execution or attachment is in the state where the corporation resides, and not in the state where the stockholder resides, or where the certificate may be found, and, in the absence of peculiar circum-

 <sup>81</sup> Burr v. Wilcox, 22 N. Y. 551, 82 Winslow v. Fletcher, 53 Conn.
 555. 390, 55 Am. Rep. 122.
 83 Supra, this section, (a).

stances, they cannot be taken in execution or attachment in any other state.84 Shares of stock cannot be taken on execution or attachment by levying upon or seizing the certificate only, and a court can acquire no jurisdiction over stock by virtue of an attachment merely because the certificate of stock is within its jurisdiction.85

There was a late decision in the United States circuit court of appeals which is at variance with this principle. In the case referred to it was held that, although certificates of stock are "technically"86 only written evidence of interests in the corporate property, they are so far in the nature of chattels that, when certificates of stock in a corporation of one state are held in pledge or as collateral in another state, the courts of the latter state may establish a lien thereon (meaning, as the decision shows, a lien on the stock represented by the certificate) in a suit commenced by substituted service under a statute authorizing such service in suits to establish liens on personal property within the state.87 It may be that, under the statute referred to, the court could acquire a lien on the certificates within its jurisdiction, regarded as property distinct from the shares of stock which they represented, and which had a situs in another state, where the corporation was, but a lien on the certificates could not give a lien on the shares, which were beyond the jurisdiction of the court, or give the court any jurisdiction to direct

<sup>84</sup> Ante, § 377.

<sup>35</sup> Am. St. Rep. 691; Christmas v. Biddle, 13 Pa. St. 223; Winslow v. Fletcher, 53 Conn. 390, 55 Am. Rep. 122; Plimpton v. Bigelow, 93 N. Y. 592, 1 Keener's Cas. 855. And see Wis. 644. ante, § 377.

held that, since certificates of stock are not the stock itself, the stock is not in the possession or control of in fact and in law. one who has possession of the cerment of the person in possession of S. 1.

the certificates, under the statute 85 Armour Bros. Banking Co. v. of that state enabling a creditor to St. Louis Nat. Bank, 113 Mo. 12, reach, by garnishment of the person in possession or control thereof, property, money, credits, or effects of the debtor, etc. O. L. Packard Machinery Co. v. Laev, 100

tte, § 377.

See Certificates of stock are not In a late Wisconsin case it was merely "technically" only written evidence of interests in the corporate property, but they are so

<sup>87</sup> Merritt v. American tificates, and therefore a creditor Barge Co., 24 C. C. A. 530, 79 Fed. of an owner of shares of stock can- 228. See, however, Jellenik v. not reach the shares by garnish- Huron Copper Mining Co., 177 U.

a sale of the shares so as to bind the corporation and the owner, or conclude the courts of the state in which the corporation, and the shares, were located.88 The decision in this case resulted, as the opinion of the court seems to show, from a failure to distinguish between a certificate of stock as a paper evidencing the ownership of shares and the shares themselves. A deed conveying land is property for which replevin will lie, but it is not the land itself, and no court would think of attempting to establish a lien upon land in another state merely because the title deeds are deposited within its jurisdiction. There can be no more jurisdiction in a court to establish a lien on shares of stock in another state merely because the certificates of stock are within its jurisdiction.

In a Connecticut case, where a resident of Indiana, owning stock in a bank of that state, had pledged the certificate, with a blank power to sell and transfer the same, to a corporation in Connecticut, it was held that neither the stock nor the surplus interest therein could be reached by attachment in Connecticut. Judge Carpenter, after stating the proposition that certificates of stock are not the stock, and defining a share of stock as consisting of a set of rights and duties between the corporation and the owner of the share, said: "These rights and duties are in fact and law quite distinguishable from the certificates and the power to transfer those rights and duties. The certificate is evidence that the person therein named possesses those rights and is subject to those duties, but is not in law the equivalent of those rights and duties. They are muniments of title, but not the title itself; much less the real property. While these certificates are in themselves valuable for some purposes, and to some extent may properly be regarded as property, yet they are

592, 1 Keener's Cas. 855.

88 Plimpton v. Bigelow, 93 N. Y. authorizing jurisdiction of a nonresident defendant to be acquired by publication when he has prop-In an Ohio case it was held that erty in the state. National Bank a nonresident shareholder in a do- of New London v. Lake Shore & mestic corporation had property in Michigan Southern Ry. Co., 21 the state, by reason of his owner-Ohio St. 221. And see Smith v. ship of shares, within a statute Pilot Mining Co., 47 Mo. App. 409. distinct from the holder's interest in the capital stock of the corporation, and are not goods and effects within the meaning of the statute relating to foreign attachment. They are no more subject to an attachment or a trustee process than a promissory note. The debt is subject to attachment, but the note itself, which is simply evidence of the debt, is not. So with stock. That may be attached, but the certificates cannot be. \* \* \* The bank is a foreign corporation. No part of its capital or property is within the jurisdiction of this court. The certificates and authority to transfer are held by one of our citizens; but we cannot through them reach the stock or take any action relative thereto which the authorities of the bank or the courts of Indiana are bound to respect." \*\*

(i) Matters elsewhere treated.—In this section, the purpose has been to treat merely of the nature of certificates of stock, and of those questions which depend upon or illustrate their nature. In subsequent sections we shall deal with the power of a corporation to issue certificates, and their form, of the right of stockholders to a certificate, and their remedies on refusal of the corporation to issue the same, the rights and liabilities growing out of forged certificates, and certificates issued illegally or by mistake, or by officers or agents fraudulently or without authority, and other questions relating to certificates of stock.

#### § 379. Conversion of shares of stock.

(a) In general.—Because of the fact that shares of stock, although personal property, 93 are intangible, it has been held in Pennsylvania that trover will not lie for the conversion of shares of stock, although it will lie for conversion of the certificate of stock which represents the shares. 94 In other jurisdictions, however, it is the settled doctrine that shares of stock, since they

<sup>89</sup> Winslow v. Fletcher, 53 Conn.

<sup>390, 55</sup> Am. Rep. 122.

<sup>90</sup> Post, § 423 et seq. 91 Post, §§ 425, 426.

<sup>92</sup> Post, § 428 et seq.

<sup>93</sup> Ante, § 376(b).

 <sup>&</sup>lt;sup>94</sup> Neiler v. Kelley, 69 Pa. St.
 403, 407; Sewall v. Lancaster Bank, 17 Serg. & R. (Pa.) 285;
 Biddle v. Bayard, 13 Pa. St. 150.

are personal property, may be the subject of a conversion, notwithstanding their intangible nature, and that the action of trover will lie to recover damages for their conversion, the declaration or complaint alleging a conversion, not merely of the certificate of stock which is evidence of the stock, but of the stock itself.<sup>95</sup>

(b) What constitutes a conversion.—Any act of dominion wrongfully exerted over another's property, in denial of his right, or inconsistent with it, may be treated as a conversion; and this is just as true of shares of stock as it is of other property. And the conversion may be either by the corporation itself, or by some third person. To maintain an action of trover for the conversion of shares of stock, the plaintiff must prove a technical conversion of the stock by the defendant; and there is no conversion unless the plaintiff had title to the stock at the time of the acts relied upon as a conversion, and such acts were wrongful, and such as to deprive him of the same, either permanently and absolutely, or partially or temporarily. 97

95 McAllister v. Kuhn, 96 U. S. 87, affirming 1 Utah, 275; Anderson v. Nicholas, 28 N. Y. 600; Mahaney v. Walsh, 16 App. Div. (N. Y.) 601; Jarvis v. Rogers, 15 Mass. 389; Maryland Fire Ins. Co. v. Dalrymple, 25 Md. 242; Ayres v. French, 41 Conn. 142; Payne v. Elliot, 54 Cal. 339, 35 Am. Rep. 80; Ralston v. Bank of California, 112 Cal. 208; Bank of America v. Mc-Neil, 10 Bush (Ky.) 54; Boylan v. Huguet, 8 Nev. 352; Sturges v. Keith, 57 Ill. 451, 11 Am. Rep. 28; Morton v. Preston, 18 Mich. 60; Feige v. Burt, 118 Mich. 243, 74 Am. St. Rep. 390; Daggett v. Davis, 53 Mich. 35, 51 Am. Rep. 91; Hubbell v. Blandy, 87 Mich. 209, 24 Am. St. Rep. 154; Carpenter v. American Building & Loan Ass'n, 54 Minn. 403, 40 Am. St. Rep. 345; Allen v. American Building & Loan Ass'n, 49 Minn. 544, 32 Am. St. Rep. 574; Connor v. Hillier, 11 Rich. Law (S. C.) 193; Nabring v. Bank of Mobile, 58 Ala. 204;

mingham, 87 Ala. 644; Budd v. Multnomah Street R. Co., 15 Or. 413, 3 Am. St. Rep. 169.

96 Carpenter v. American Building & Loan Ass'n, 54 Minn. 403, 40 Am. St. Rep. 345; Mahaney v. Walsh, 16 App. Div. (N. Y.) 601; and cases cited in the notes following.

97 Daggett v. Davis, 53 Mich. 35,
 51 Am. Rep. 91.

Where stock is loaned to a person to sell the same, and use the proceeds in his business, and he does so, but afterwards refuses or fails to return the stock or account, he is not liable to an action of trover. The relation between the parties is simply that of debtor and creditor. Borland v. Stokes, 120 Pa. St. 278.

54 Minn. 403, 40 Am. St. Rep. 345; Allen v. American Building & Loan Ass'n, 49 Minn. 544, 32 Am. St. Rep. 574; Connor v. Hillier, 11 each, to be sold for the benefit of Rich. Law (S. C.) 193; Nabring v. Bank of Mobile, 58 Ala. 204; not back out after the rest have Sharpe v. National Bank of Bircontributed their portions; and if

In order that conversion of a certificate of stock may constitute a conversion of the stock which it represents, the owner must be thereby deprived of the stock, and not merely of the certifi-It has been held, therefore, that conversion of an unindorsed certificate of stock is not a conversion of the stock, and gives a right of action, not for the value of the stock, but for nominal damages only.98

When a person is lawfully in possession of stock, a demand is necessary before an action of trover can be maintained against him.99

---Conversion by the corporation.--A corporation, as we shall hereafter see more at length, is guilty of a conversion of stock if it sells or declares a forfeiture thereof for nonpayment of assessments, when it has no right to sell or forfeit the same, or where, although it may have such right, it fails to comply with charter or statutory provisions as to the mode of sale or forfeiture, etc., and afterwards refuses to recognize the owner as a stockholder. In such a case he may maintain an action against the corporation for conversion, and recover the value of the stock as damages.<sup>100</sup> A corporation may also be guilty of a conversion of the stock if it wrongfully refuses to recognize a valid transfer, and to register the transfer, and issue a new certificate

shares are used in accordance with the agreement, he cannot bring trover for them. Conrad v. La

Rue, 52 Mich. 83. Where a special administrator of an estate, as such, and without authority, sells shares of stock in a corporation which had been pledged to the deceased in his lifetime as security for a loan of money, and receives the proceeds, which he pays over to the executors, this is not a conversion of the stock by the estate, so as to enable the pledgor to maintain trover. His remedy is an action for money had and received. Von Schmidt Bourn, 50 Cal. 616.

When the title to shares of stock

he attempts to do so, and his is, under a will, in a cestui que trust, the trustee, being directed merely to collect and pay over dividends, cannot maintain an action of trover for their conversion. Onondaga Trust & Deposit Co. v. Price, 87 N. Y. 542; White v. Price, 39 Hun (N. Y.) 394, 108 N. Y. 661.

98 Daggett v. Davis, 53 Mich. 35, 51 Am. Rep. 91.

99 Moynahan v. Prentiss, 10 Colo. App. 295.

100 Budd v. Multnomah Street R. Co., 15 Or. 413, 3 Am. St. Rep. 169; Allen v. American Building & Loan Ass'n, 49 Minn. 544, 32 Am. St. Rep. 574; Carpenter v. American Building & Loan Ass'n, 54 Minn. 403, 40 Am. St. Rep. 345. See post, § 495.

to the transferee.<sup>101</sup> When stock is converted by the corporation, the owner may maintain trover to recover damages for the conversion, without returning or offering to return his certificate of stock.<sup>102</sup>

Conversion by third person.—As was stated above, shares of stock may be converted by a third person, as well as by the corporation. Any wrongful use of a certificate of stock, bearing an executed assignment and power to transfer the same, so as to procure the title to be vested in a person not entitled, or otherwise deprive the owner of his property in the stock, may be treated as a conversion, and sued upon as such, notwithstanding the fact that the certificate is not the stock itself. 103

Where the holder of a certificate of stock transfers part of the shares represented thereby by an instrument in writing, and afterwards, before the transfer is entered on the books of the corporation, transfers all of the shares represented by the certificate to another party, he wrongfully exercises an active dominion over the shares first transferred, and converts the same. Where the widow and heirs of a stockholder, thinking to avoid the expense of administration, took his certificate of stock and indorsed their names upon it, and left it with one of their number to be sold for the benefit of all, and the person with whom it was left, instead of selling it, pledged it for his own debt, and the pledgee was recognized by the corporation as the owner of the stock, and disposed of it as owner, it was held that an administrator subsequently appointed could maintain an action against the pledgee for conversion of the

<sup>101</sup> Bond v. Mt. Hope Iron Co.,
99 Mass. 505, 97 Am. Dec. 49; Craig
v. Hesperia Land & Water Co., 113
Cal. 7, 54 Am. St. Rep. 316. See
post, § 603.

<sup>&</sup>lt;sup>102</sup> Carpenter v. American Building & Loan Ass'n, 54 Minn. 403, 40 Am. St. Rep. 345.

<sup>103</sup> McAllister v. Kuhn, 96 U. S.
87, affirming 1 Utah, 275; Sturges
v. Keith, 57 Ill. 451, 11 Am. Rep.
28.

In Hubbell v. Blandy, 87 Mich. 209, 24 Am. St. Rep. 154, it was held that a gratuitous bailee of stock is liable for its conversion, if, without authority from the owner, he delivers the certificate to the officers of the corporation, who cancel it, and issue a new certificate to another person, although he may have acted in good faith, and on a forged order.

<sup>&</sup>lt;sup>104</sup> Mahaney v. Walsh, 16 App. Div. (N. Y.) 601.

stock. 105 Shares of stock, as we shall see more at length in a subsequent chapter, may be converted by a pledgee, as by selling the same without notice to the pledgor. 106 A tax collector is liable in trover for wrongfully selling stock for an illegal tax. 107

(c) Measure of damages for conversion of stock.—It is agreed that the plaintiff in an action for the conversion of shares of stock is entitled to recover as his damages a sufficient sum to compensate him for his actual loss, and that he is not entitled to recover more than this. 108 But as to the proper measure of damages, when the plaintiff has been wholly deprived of his stock, there has been some difference of opinion. In England it has been held in some cases that the measure of damages is the Value of the stock at the time of the trial in the action for conversion.109 And in this country, in some of the cases, it has been held to be the highest value of the stock between the time of the conversion and the time of the trial or verdict. 110 most jurisdictions, however, it is now settled that the proper measure of damages is, with the addition of the elements hereafter stated, the value of the stock at the time of the conversion, or within a reasonable time after the plaintiff's discovery of the conversion, in which he might have purchased other shares, and thus placed himself in statu quo. 111 A broker or other agent

106 Feige v. Burt, 118 Mich. 243, 74 Am. St. Rep. 390. See post, §

107 Sprague v. Fletcher, 69 Vt. 69. 108 Daggett v. Davis, 53 Mich. 35, 51 Am. Rep. 93, and other cases in the notes following.

109 Shepherd v. Johnson, 2 East, McArthur v. Seaforth, 2 Taunt. 257; Downes v. Back, 1 Starkie, 318; Harrison v. Harrison, 1 Car. & P. 412; Owen v. Routh, 14 C. B. 327. But see In re Bahia & San Francisco R. Co., L. R. 3 Q. B. 584, 2 Smith's Cas. 1092; Shaw v. Holland, 15 Mees. & W. 136.

105 Morton v. Preston, 18 Mich. 50 Ga, 444; Kid v. Mitchell, 1 Nott & McC. (S. C.) 334, 9 Am. Dec. 702.

The earlier cases in New York and Pennsylvania adopted this rule. Markham v. Jaudon, 41 N. Y. 235; Romaine v. Van Allen, 26 N. Y. 309; Bank of Montgomery v. Reese, 26 Pa. St. 143; Reitenbaugh v. Ludwick, 31 Pa. St. 131; Musgrave v. Beckendorff, 53 Pa. St. 310. These decisions, however, been overruled. See the New York and Pennsylvania cases cited in note 111. infra.

As to the measure of damages in California, see note 113, infra.

111 Sturges v. Keith, 57 Ill. 451, olland, 15 Mees. & W. 136. 11 Am. Rep. 28; Brewster v. Van 110 See Central Railroad & Bank-Liew, 119 III. 554, 59 Am. Rep. 823; ing Co. v. Atlantic & Gulf R. Co., Boylan v. Huguet, 8 Nev. 345; Berwho, without the knowledge of his principal, and in violation of his trust, receives and retains for his own benefit stock delivered in part payment of a contract made on behalf of his principal, or who otherwise converts stock held by him for his principal, is chargeable with the highest market value of the stock between the time of the conversion and a reasonable time after discovery thereof by the principal, in which the principal might have placed himself in statu quo by purchasing the stock. 112 In some jurisdictions there are statutory provisions on the subject.113

cich v. Marye, 9 Nev. 312; Citi- Grat. (Va.) 366; Noonan v. Ilsley, zens' Street R. Co. v. Robbins, 144 17 Wis. 314, 84 Am. Dec. 742. zens' Street R. Co. v. Robbins, 144 Ind. 671; Wright v. Bank of Metropolis, 110 N. Y. 237, 6 Am. St. Rep. 356; Baker v. Drake, 53 N. Y. 211, 13 Am. Rep. 507, 66 N. Y. 518, 23 Am. Rep. 80; Ormsby v. Vermont Copper Min. Co., 56 N. Y. 623; Barnes v. Brown, 130 N. Y. 372; Smith v. Savin, 141 N. Y. 315; Hubbell v. Blandy, 87 Mich. 209, 24 Am. St. Rep. 154; Freeman v. Harwood, 49 Me. 195; Darling v. Potts, 118 Mo. 506; Brinkerhoff-Farris Trust & Savings Co. v. Home Lumber Co., 118 Mo. 447; Pinkerton v. Manchester & Lawrence R. Co., 42 N. H. 424; Work v. Bennett, 70 Pa. St. 484; Pennsylvania Co. for Insurance on Lives v. Philadelphia, Germantown & N. R. Co., 153 Pa. St. 160; Connor v. Hillier, 11 Rich. Law (S. C.) 193, 73 Am. Dec. 105.

And see Jefferson v. Hale, 31 Ark. 286; Fisher v. Brown, 104 Mass. 259, 6 Am. Rep. 235; Eastern R. Co. v. Benedict, 10 Gray (Mass.) 212; Wyman v. American Powder Co., 8 Cush. (Mass.) 168; Sargent v. Franklin Ins. Co., 8 Pick. (Mass.) 90, 19 Am. Dec. 306; McKenney v. Haines, 63 Me. 74; White v. Salisbury, 33 Mo. 150; Huntingdon & B. T. Railroad & Coal Co. v. English, 86 Pa. St. 247; Coal Co. v. English, 86 Pa. St. 241; shares at the time of hing the offic. North v. Phillips, 89 Pa. St. 250; Fowle v. Ward, 113 Mass. 548, 18 Bull v. Douglas, 4 Munf. (Va.) Am. Rep. 534.

303; Enders v. Board of Public Works, 1 Grat. (Va.) 364; Orange 112 Galigher v. Jones, 129 U. S. 193; McKinley v. Williams (C. C. & Alexandria R. Co. v. Fulvey, 17 A.) 74 Fed. 94; Baker v. Drake, 53

See, also, In re Bahia & San Francisco R. Co., L. R. 3 Q. B. 584, 2 Smith's Cas. 1092; Shaw v. Holland, 15 Mees. & W. 136.

The measure of damages is not the highest market value between the conversion and the trial. Boylan v. Huguet, 8 Nev. 345; Baker v. Drake, 53 N. Y. 211, 13 Am. Rep. 507; and other cases above cited.

Nor is it the market value of the stock at the time of the trial, together with cash dividends previously declared. Sturges v. Keith, 57 Ill. 451, 11 Am. Rep. 28.

The plaintiff cannot recover the price which he paid for the stock, if greater than its value at the time of the conversion. Brewster v. Van Liew, 119 Ill. 554, 59 Am. Rep. 823.

Where one with whom shares have been pledged as collateral wrongfully sells the same for the full market price, and the pledgor files a bill in equity to redeem, his recovery is not limited to the damages which he might recover in an action of trover, but he is entitled to be placed in the same position as if the sale had not been made, and the defendant, therefore, may be charged with the value of the shares at the time of filing the bill.

The value of shares of stock for the purpose of ascertaining the damages for its conversion is not necessarily its par value. but it is its actual value, whether above or below par. 114 It is not the market value, if it appears that the actual value was different.115 But the market value, if there was any, is to be taken as the actual value, in the absence of evidence to the con-If it had no market value, the actual value is to be proven by other evidence. 117 In the absence of any evidence

N. Y. 211, 13 Am. Rep. 507, 66 N. Y. 518, 23 Am. Rep. 80; Gruman v. Smith, 81 N. Y. 26; Colt v. Owens, 90 N. Y. 368; Wright v. Bank of Metropolis, 110 N. Y. 237, 6 Am. St. Rep. 356; Smith v. Savin, 141 N. Y. 315; Citizens' Street R. Co.

v. Robbins, 144 Ind. 671.

Where lands owned in partnership were sold by some of the partners for shares of stock, for which they failed to account to the other partner, it was held that the measure of the latter's damages for the conversion of the stock was the highest market value between the date of the conversion and the time when he acquired knowledge Morris v. Wood (Tenn. thereof. Ch. App.) 35 S. W. 1013.

113 In California it is provided by statute: "The detriment caused by the wrongful conversion of personal property is presumed to be: (1) The value of the property at the time of the conversion, with the interest from that time; or, where the action has been prosecuted reasonable diligence, highest market value of the property at any time between the conversion and the verdict, without interest, at the option of the injured party; and (2) a fair compensation for the time and money properly expended in pursuit of the property." Civ. Code, § 3336, as amended in 1878. This statute applies to the conversion of shares of stock, as well as other personal property.

Page v. Fowler, 39 Cal. 412, 2 Am. Rep. 462; Thompson v. Toland, 48 Cal. 99; Tulley v. Tranor, 53 Cal. 274; Dent v. Holbrook, 54 Cal. 145; Fromm v. Sierra Nevada Silver Min. Co., 61 Cal. 629; Ralston v. Bank of California, 112 Cal. 208.

114 See Freon v. Carriage Co., 42 Ohio St. 30, 51 Am. Rep. 794; State v. Carpenter, 51 Ohio St. 83, 46 Am. St. Rep. 556. See, also, Bull v. Douglas, 4 Munf. (Va.) 303; Enders v. Board of Public Works, 1 Grat. (Va.) 364; and other cases cited in the notes follow-

115 Freon v. Carriage Co., 42 Ohio St. 30, 51 Am. Rep. 794; State v. Carpenter, 51 Ohio St. 83, 46 Am. St. Rep. 556. See Redding v. Godwin, 44 Minn. 355.

116 Sturges v. Keith, 57 Ill. 451, 11 Am. Rep. 28; Darling v. Potts, 118 Mo. 506; and other cases above

The market value of stock is the actual price at which it is commonly sold. That price may be fixed by sales of the stock in market at or about a given time. If no sales can be shown on the precise day, recourse may be had to sales before or after such day, and for that inquiry a reasonable range in point of time is allowable. Douglas v. Merceles, 25 N. J. Eq.

117 Brinkerhoff-Farris Trust & Savings Co. v. Home Lumber Co., 118 Mo. 447; Moffitt v. Hereford, 132 Mo. 513; Brown v. Lawton, 6 For cases in California, see N. Y. Supp. 137; Pabst Brewing Co. Douglass v. Kraft, 9 Cal. 562; Hav. v. Montana Brewing Co., 19 Mont. mer v. Hathaway, 33 Cal. 117; 294; Hitchcock v. McElrath, 72 as to the actual value, it will be presumed that the par value was the actual value.118

In addition to the value of the stock, the plaintiff is entitled to recover any special damages resulting proximately from the conversion, and which he alleges and proves. 119 He is entitled to interest on the value of the stock from the time of the conversion to the time of the verdict. 120 And he is entitled to recover the amount of any dividends received by the defendant

Colo. App. 295.

If there is no market value, proof may be given of transactions in the particular stock, sales, options, and prices at which such stock has been sold or optioned, and at which it can be sold or optioned. Moynahan v. Prentiss, 10 Colo. App. 295, 302; Kuhn v. Mc-Kay, 7 Wyo. 42. See, also, Smith v. Traders' National Bank, 82 Tex.

Actual value of stock may be established by proof of its dividendearning capacity, or the value of its assets, or individual sales of stock not under compulsion. Brinkerhoff-Farris Trust & Savings Co. v. Home Lumber Co., 118 Mo. 447; Hewitt v. Steele, 118 Mo. 463; Greer v. Lafayette County Bank, 128 Mo. 559.

Actual value of the stock of a corporation "may be shown by proof of the value of the property and business of the corporation, its good will, and dividend-earning capacity." State v. Carpenter, 51 Ohio St. 83, 46 Am. St. Rep. 556. See, also, Freon v. Carriage Co., 42 Ohio St. 30, 51 Am. Rep.

The value of the corporate assets, the dividends paid, the permanency of the business, the control of the stock, and other circumstances of a like nature, may be taken into consideration. Moffitt v. Hereford, 132 Mo. 513. And see Nelson v. First Nat. Bank of Killingley (C. C. A.) 69 Fed. 798.

Cal. 565: Movnahan v. Prentiss. 10 placed in the hands of a receiver in proceedings for its dissolution as insolvent, see Nelson v. First Nat. Bank of Killingley (C. C. A.) 69 Fed. 798.

> A finding that the value of stock on a certain day was much below its previous value, or was of no value, is not justified by the mere fact that there was no market sale for it on such day. Pabst Brewing Co. v. Montana Brewing Co., 19 Mont. 294.

> The condition of the assets and liabilities of a corporation at a certain time does not tend to show the value of its stock four years earlier, in the absence of anything to connect the two periods. v. Ellis' Estate, 68 Vt. 544.

> 118 Harris' Appeal (Pa. Sup. Ct.) 12 Atl. 743; Moffitt v. Hereford, 132 Mo. 513.

119 Boylan v. Huguet, 8 Nev. 345. 120 Sturges v. Keith, 57 Ill. 451, 11 Am. Rep. 28; Boylan v. Huguet, 8 Nev. 345; O'Meara v. North American Min. Co., 2 Nev. 112; Freeman v. Harwood, 49 Me. 195; Hubbell v. Blandy, 87 Mich. 209, 24 Am. St. Rep. 154; Pinkerton v. Manchester & Lawrence R. Co., 42 N. H. 424; North v. Phillips, 89 Pa. St. 250; White v. Smith, 54 N. Y. 522; Ormsby v. Vermont Copper Min. Co., 56 N. Y. 623; Darling v. Potts, 118 Mo. 506.

And see Bull v. Douglas, 4 Munf. (Va.) 303; Enders v. Board of Public Works, 1 Grat. (Va.) 364; Huntingdon & B. T. Railroad & As to proof of the value of stock Coal Co. v. English, 86 Pa. St. 247; in a corporation which has been McKenney v. Haines, 63 Me. 74.

upon the stock up to the time of the conversion, with interest thereon to the time of the trial. 121

If the plaintiff has sustained no actual damages, because the stock was of no value at all, or was returned to him, or for any other reason, he can recover nominal damages, and such damages only. 122 If a certificate of stock only, as distinguished from the stock, is converted, the action must be for conversion of the certificate, and the measure of damages is not the value of the stock, but the value of the certificate only, which is generally merely nominal.123

In an action for the conversion of stock by one to whom it was pledged as security for a debt, the amount due the defendant is to be deducted. 124 And when shares are converted by the corporation by an unauthorized or invalid forfeiture or sale for nonpayment of assessments, the measure of damages is not the value of the shares, but their value less the amount due thereon.125

--- Return or offer to return stock.-The return of the stock after an action is brought for its conversion, or after the conversion, and before action, does not defeat the action, but merely affects the measure of damages, which will be merely nominal unless actual damages are proved. 126 The plaintiff is not bound

121 Hubbell v. Blandy, 87 Mich. Budd v. Multnomah Street R. Co., 209, 24 Am. St. Rep. 154; Balti- 15 Or. 413, 3 Am. St. Rep. 169; more City Passenger R. Co. v. Fosdick v. Greene, 27 Ohio St. 484, Sewell, 35 Md. 238, 6 Am. Rep. 22 Am. Rep. 328. 402; Freeman v. Harwood, 49 Me. 195; Bercich v. Marye, 9 Nev. 312; Bank of Montgomery v. Reese, 26 Pa. St. 143.

But where the plaintiff recovers as damages the value of the stock at the time of the conversion, or a reasonable time thereafter, he is not entitled to also recover the amount of dividends, or interest thereon, which accrued after such time. Citizens' Street R. Co. v. Robbins, 144 Ind. 671.

122 Daggett v. Davis, 53 Mich. 35,

123 Daggett v. Davis, 53 Mich. 35. 51 Am. Rep. 91.

124 Work v. Bennett, 70 Pa. St.

125 Budd v. Multnomah Street R. Co., 15 Or. 413, 3 Am. St. Rep. 169. 126 Carpenter v. American Build-

ing & Loan Ass'n, 54 Minn. 403, 40 Am. St. Rep. 345,

But if the plaintiff in an action to recover the value of personal property wrongfully converted does accept a return of the property, he cannot recover damages for time 51 Am. Rep. 91; McLean v. Charles and trouble and expenses incurred Wright Medicine Co., 96 Mich. 479; in obtaining the return of the to accept an offer to return the stock before action is brought, and such an offer does not defeat his right of action, nor mitigate the damages.<sup>127</sup>

#### II. ISSUE OF STOCK AND PAYMENT THEREFOR.

§ 380. In general.—It has been held that a corporation has no power to create a capital stock and issue shares, unless the power has been expressly conferred by the legislature; but it is doubtful whether this is true in all cases. It has no such power if a capital stock is inconsistent with its nature and objects.

Stock may be issued, subject to express charter or statutory restrictions, in the following ways:

- (1) Upon subscriptions for shares of original capital stock.
- (2) Upon a sale thereof by the corporation.
- (3) Upon subscription or sale after an authorized increase of the capital stock.
- (4) By making a stock dividend from profits available for the payment of dividends.
- (5) By pledge of the same as collateral security for a valid debt. In the absence of express charter, statutory, or constitutional restrictions, a corporation may accept payment for stock either in money or its equivalent. Thus:
  - (1) It may take payment in cash.
- (2) It may take property, labor, or services, provided it would have the power to purchase the property, or incur a debt for the labor or services.
- (3) It may take unsecured notes or bonds, or notes or bonds secured by a mortgage on real or personal property.
  - (4) It may issue stock in payment of a valid debt.
- (5) It may issue stock by way of pledge as collateral security for a valid debt, whether previously contracted, or contracted at the time of the pledge.

# § 381. Power of corporation to create and issue stock.

When it is intended to create or authorize the formation of a

same. Collins v. Lowry, 78 Wis.

127 Carpenter v. American Building & Loan Ass'n, 54 Minn. 403, 40
Am. St. Rep. 345.

joint-stock corporation, the legislature generally, if not always, expressly provides for the creation of a fixed capital stock, and the issue of shares thereof. Whether such power can ever exist without express authority is not clear. All the definitions of "capital stock" assume that it is provided for or authorized by the legislature, 128 and it is well settled, as we shall hereafter see, that when the amount of the capital stock of a corporation is fixed by the legislature, the corporation has no power to increase or reduce the same without legislative authority; 129 but it seems that until recently there has never been a direct decision on the question whether a corporation can create a capital stock, so as to become a joint-stock corporation, and issue shares thereof, when it is not expressly authorized to do so by the legislature, or, in other words, whether such power can ever be implied when not withheld. In a late Pennsylvania case, the question was decided in the negative. In this case the legislature had, by a special act, created certain persons, and other persons who might become their associates, a corporation for the purpose of establishing and maintaining a cemetery, for profit, with authority to purchase the necessary land within certain limits as to acreage, and to lay it out into lots and dispose of the same, etc., but nothing was said one way or the other as to the creation of a capital stock. It was held that, since there was no express authority for creating a capital stock, and since a capital stock was not necessary to enable the corporation to accomplish its authorized objects, so that its creation might be regarded as among the powers impliedly granted, there was no power whatever to create a capital stock and issue shares. The court said, after referring to authorities holding it ultra vires for a corporation to increase or reduce its capital stock without legislative authority: "It is extremely difficult to understand, under the foregoing decisions, how any issue of capital stock by this company can be regarded as valid. The company was chartered to establish a cemetery. While a cemetery company is not necessarily a religious or charitable corporation, yet in many instances it is of that character, and perhaps as a rule this is so. Yet they may be established as merely private enterprises, and carried on for profit. But in either case, if the charter confers no right or power to create capital stock, it is difficult to understand how any right to create and issue such stock has any existence. If capital stock may neither be increased nor diminished without an express power to that effect, how can any stock be created or issued when there is no capital stock fixed by the charter, and no power is given to create it? If the doctrine of these cases be true, and the act of increasing or decreasing the capital stock of a corporation with specific charter power to do so, is a void act, because it is ultra vires, how can it be true that a corporation may issue any capital stock without having specific legislative authority to do so? We cannot see. If it is ultra vires to increase, it is ultra vires to issue any stock where no power to do so is conferred by the The power to create corporate capital stock is a legislative function, and in any given case, in order that such stock may have a legal existence, the function must be exercised."130

The soundness of this decision may well be doubted. From the doctrine that a corporation cannot, without legislative authority, increase the amount of its capital stock when it is fixed by the legislature, or by the articles of association in pursuance of legislative authority, it does not necessarily follow that a corporation cannot create a capital stock without express authority. The legislature may certainly expressly authorize a corporation to create a capital stock and leave it for the stockholders, in the articles of association, to fix the amount thereof, and this is often done. When the amount is so fixed, it becomes the authorized amount of the capital stock, which cannot be increased or reduced without legislative authority. Now, if the legislature creates or authorizes the formation of a corpora-

<sup>&</sup>lt;sup>130</sup> Cooke v. Marshall, 191 Pa. St. See, also, Detroit Chamber of Com-315; on rehearing, 196 Pa. St. 200. merce v. Gardner, 109 Mich. 691.

tion for profit, without saying anything at all as to the creation of a capital stock, and the issue of stock is an appropriate mode of raising the necessary capital, and fixing and evidencing the respective interests of the members of the corporation, there is no good reason why it cannot be held that the corporation has the implied power to create a capital stock to such an amount as may be reasonably necessary to enable it to accomplish the objects for which it was created. 131 The fact that it is possible for the corporation to carry out its objects without a capital stock is not a good objection to this view, for a power, to be implied, need not be necessary in the sense of "indispensable." It is enough if it be obviously appropriate and convenient. "Power necessary to a corporation does not mean simply power which is indispensable. Such phraseology has never been interpreted in so narrow a sense. A power which is obviously appropriate and convenient to carry into effect the franchise granted, has always been deemed a necessary one. The term comprises a grant of the right to use all the means suitable and proper to accomplish the end which the legislature had in view, at the time of the enactment of the charter."132

Of course, a corporation cannot create a capital stock and issue shares when a capital stock is inconsistent with its nature, as fixed by the act creating it. Where a statute incorporating a savings bank provided that the corporation might receive on deposit, for the use and benefit of depositors, money offered for that purpose, and invest the same in the manner provided by the statute, and that the income from the deposits should be divided among the depositors or their legal representatives according to the terms stipulated, it was held that the corporation was not authorized to issue or create capital stock, since the profits, after deducting necessary expenses, inured entirely to

<sup>131</sup> See the dissenting opinion of Mitchell, J., concurred in by Serrett., C. J., and Fell, J., in Cooke v. Law, 545. And see ante, § 128(e) Marshall, 196 Pa. St. 200.

the benefit of the depositors, either as dividends or reserved surplus.133

# § 382. How stock may be issued.

By the "issue of stock," as the expression is here used, is meant the act or contract of the corporation by which shares of its capital stock are vested in persons as stockholders or members, and not merely the issue of certificates of stock, which, as we have seen, are not the stock itself, but merely evidence of the ownership of stock, and the rights of the owner as a stock-There are several ways in which stock may be isholder.134 sued by a corporation:

- (1) The usual mode is upon subscriptions therefor, made either before or after the corporation is organized. when it is proposed to organize a corporation, a paper is signed by a number of persons, by which they promise to take a certain number of shares in the corporation when formed. The corporation is then formed, and expressly or impliedly accepts the subscriptions, and upon such acceptance they become binding contracts between the corporation and the subscribers, making the subscribers members or stockholders in the corporation to the extent of their subscriptions, and giving them all the rights, and subjecting them to all the liabilities, which attach to stockholders. 135 Certificates of stock are usually issued to the subscribers as evidence of their rights, but, as has been stated, they are not necessary to make them stockholders. 186 Subscriptions for stock may also be received by a corporation after it has been formed, provided it has unissued stock, and the subscribers will become stockholders as soon as the subscriptions are accepted.137
- (2) Înstêad of issuing its stock upon subscriptions, a corporation, after it has been formed, may sell its unissued stock for money, or exchange it for property, labor, or services, or issue

<sup>188</sup> Huntington v. National Savings Bank, 96 U.S. 388.

<sup>135</sup> Post, § 439(c). 136 Ante, § 378. 137 Post, § 439(b).

<sup>134</sup> Ante. § 378.

it in payment of a valid debt which it has contracted.<sup>138</sup> Stock issued by a corporation, but reacquired lawfully by surrender, forfeiture, or purchase, may be reissued by selling the same.<sup>139</sup> A sale of stock and a subscription for stock are to some extent governed by different rules. Thus, as we have elsewhere seen, an action may generally be maintained by a corporation on a subscription without issuing or tendering a certificate, whereas, if it has sold stock, it must issue or tender a certificate before it can maintain an action for the price.<sup>140</sup> Whether or not a particular transaction is a subscription for stock or a sale of stock depends, of course, upon the terms of the contract.<sup>141</sup>

(3) After a corporation has been formed, and all of its original stock has been issued, it may, if authorized by its charter, but not otherwise, increase the amount of its capital stock, and either offer the new stock for subscription, or sell the same for money, or for property, labor, or services, or issue it in payment of debts.<sup>142</sup>

138 Van Cott v. Van Brunt, 82 N. Y. 535, 2 Keener's Cas. 954; Lake Superior Iron Co. v. Drexel, 90 N. Y. 87; Clark v. Bever, 139 U. S. 96, 2 Keener's Cas. 967; Handley v. Stutz, 139 U. S. 417, 2 Keener's Cas. 976, 2 Smith's Cas. 844, 1 Cum. Cas. 855; Kohlmetz v. Calkins, 16 App. Div. (N. Y.) 518; Considerant v. Brisbane, 14 How. Pr. (N. Y.) 487.

139 Southern Life Ins. & Trust Co. v. Lanier, 5 Fla. 110, 58 Am. Dec. 448. And see post, §§ 390(c), 401(h).

140 Ante, § 378(b).

141 See Walter A. Wood Harvester Co. v. Jefferson, 71 Minn. 367; Lincoln Shoe Mfg. Co. v. Sheldon, 44 Neb. 279; Kohlmetz v. Calkins, 16 App. Div. (N. Y.) 518; Wemple v. St. Louis, Jerseyville & S. R. Co., 120 III. 196.

A contract reciting: "We, the cont undersigned, severally subscribe and for and agree to take and pay for the number of shares set opposite our names, respectively," of a certain corporation, providing that

"these subscriptions shall become binding" as soon as stock to a certain amount shall be subscribed, and that "payment on the subscriptions shall be made in installments as called for by the board of directors," etc., is not a sale of stock, but a subscription for stock, and tender of a certificate is not necessary before suing thereon. Walter A. Wood Harvester Co. v. Jefferson, 71 Minn, 367.

In a Nebraska case, a writing reciting: "For value received, we, the undersigned subscribers, hereby bind ourselves to purchase the number of shares of stock set opposite our respective names \* \* \* at fifty dollars per share; onefourth of the amount so subscribed \* \* \* to be paid when the foundation of the building is laid; \* \* \* and the balance on call of the directors,"-was held evidence of a contract of subscription for stock, and not of a contract of purchase from the corporation. from the corporation. Lincoln Shoe Mfg. Co. v. Sheldon, 44 Neb.

142 See post, § 405 et seg.

- (4) Another mode in which a corporation may issue stock is by making a stock dividend. As we shall see at length in another chapter, if a corporation has in reserve stock which it can lawfully issue, or if it is authorized to increase its capital stock, it may, subject to some limitations, retain surplus profits in its business, or as a surplus fund to meet future needs, instead of dividing them among the stockholders as a dividend in cash or property, and pay a dividend by-issuing reserved or additional stock.143
- (5) As we shall see in a subsequent section, a corporation, in the absence of express restriction, may pledge its unissued stock as collateral security for a debt previously contracted, or contracted at the time of the pledge.

# § 383. Payment for stock in general.

In the absence of an express charter or statutory requirement, the stock of a corporation need not be paid in in cash at the time of its organization, or within any particular time after its organization, but assessments or calls may be made upon the subscribers, as the money is needed. 144 Neither payment nor the issue of a certificate is necessary, in the absence of an express provision, to make one a stockholder, with all the rights and subject to all the liablities of a stockholder.145

Sometimes, however, there are express charter or statutory provisions requiring the whole amount of the capital stock to be paid in before the commencement of business, or within a certain time after the organization of the corporation; and a failure to comply with such a provision may render the charter of the corporation subject to forfeiture in proceedings by the

<sup>143</sup> Post, § 523(e).

<sup>144</sup> See post, § 497 et seg.

Downing v. Potts, 23 N. J. Law, 66; Savage v. Ball, 17 N. J. Eq. 142; Mitchell v. Beckman, 64 Cal. 117; 145 Cartwright v. Dickinson, 88 Glenn v. Rosborough, 48 S. C. 272. Tenn. 476, 17 Am. St. Rep. 910; See ante, § 378 (b). Compare Busey Windsor Electric Light Co. v. Tanv. Hooper, 35 Md. 15, 6 Am. Rep. dy, 66 Vt. 248, 44 Am. St. Rep. 838; 350; McComb v. Credit Mobilier of Chaffin v. Cummings, 37 Me. 76; America, 13 Phila. (Pa.) 468.

state, or forfeit the same ipso facto, 146 or prevent the corporation from acquiring a de jure corporate existence.147

While payment for stock by subscribers is not necessary to make them stockholders, in the absence of express provision therefor, it has been held that a subscriber is not a stockholder, so as to be entitled to sue as such in equity on behalf of the corporation, where his subscription, or an installment thereof, has become due and payable, and he has refused to pay the same upon a valid call.148

The necessity for payment of a deposit at the time of subscribing for stock, and the effect of failure to do so, is elsewhere considered. 149

As we shall see more at length in subsequent sections, there may be circumstances under which a corporation may issue its stock upon payment of less than its par value, but in many jurisdictions this is expressly prohibited by the constitution or by stat-And even in the absence of an express prohibition, an agreement that stock shall be paid for at less than its par value. except under peculiar circumstances, while it may be binding as between the corporation and the subscribers or purchasers, and as against consenting or participating stockholders, is

ter of a corporation may be for scribe and pay in the capital stock feited for failure to comply with a law requiring the full capital stock to be paid up within one year from the date of its organization. People v. City Bank of Leadville, 7 Colo. 226. See, also, People v. Chambers, 42 Cal. 201.

Where an act incorporating a banking company provided that there should be a certain amount of capital stock, that no increase should be made unless the amount thereof should be paid in, that before commencement of business the stockholders should pay their subscriptions in full, and that the act should become void unless the corporation should organize and proceed to business within two years,

146 It has been held that the char- it was held that failure to subwithin two years forfeited the charter. People v. National Sav-ings Bank, 129 Ill. 618.

147 See People v. Chambers, 42 Cal. 201. And see ante, § 48(f).

Generally such requirements are conditions subsequent, and not conditions precedent, to acquiring corporate existence. See Hammond v. Straus, 53 Md. 1, 14. And see ante,

Noncompliance with such requirements does not prevent the association from being a corporation de facto. See ante, § 82(f) (5), note 195.

148 Busey v. Hooper, 35 Md. 15, 6 Am. Rep. 350.

149 Post, § 508 et seq.

fraudulent as against dissenting stockholders, and as against persons who subsequently become creditors of the corporation on the faith of its capital stock being fully paid. 150

Recovery of excessive payment.—A stockholder in a corporation, who has voluntarily paid more than par for his stock in discharge of his obligation on his subscription, cannot recover back the excess from the corporation, if the payment was not made under a mistake; nor can he recover from the other stockholders, although they may have paid less than par under an agreement between the corporation and all the stockholders.\*

## § 384. Payment for stock in property, labor, or services.

(a) In general.—It is well settled, both in England and in this country, that a corporation need not necessarily receive money in payment for its stock, unless there is some requirement to this effect in its charter, or in the constitution or general laws of the state. Whether stock is issued upon subscriptions or sold, the corporation, in the absence of express restrictions, may receive or contract to receive payment therefor in property, labor, or services, provided it would, under the express or implied powers conferred upon it by its charter, have the power to purchase the property or incur a debt for the labor or services, and provided the transaction is in good faith, and no fraud is perpetrated upon other stockholders or creditors. 151

150 See post, § 389 et seq.

As to the effect of subscriptions on special terms, see post, § 465 et

\*Esgen v. Smith (Iowa) 84 N.

151 England: Woodfall's Case, 3 De Gex & S. 63; Spargo's Case, 8 Ch. App. 407, 2 Smith's Cas. 841; Coates' Case, L. R. 17 Eq. 169; Burkinshaw v. Nicolls, 3 App. Cas. 1004; In re Wragg [1897] 1 Ch. Larocque v. Beauchemin [1897] App. Cas. 358.

art, 144 U.S. 104; Coit v. Gold Amalgamating Co., 119 U.S. 343, 2 Smith's Cas. 839, 2 Keener's Cas. 1887; Branch v. Jesup, 106 U. S. 468; Bank of Fort Madison v. Alden, 129 U. S. 372; Phelan v. Hazard, 5 Dill. 45, Fed. Cas. No. 11,-068; Foreman v. Bigelow, 4 Cliff. 508, Fed. Cas. No. 4,934; Washburn v. National Wall-Paper Co. (C. C. A.) 81 Fed. 17; Coe v. East & West R. Co., 52 Fed. 531.

Alabama: Frenkel v. Hudson, 82 Ala. 158, 60 Am. Rep. 736; Knox v. Childersburg Land Co., 86 Ala. 180; United States: Camden v. Stu- Eppes v. Mississippi, Gainesville &

This is on the ground that there is no need for the roundabout process of first issuing the stock for money, and then paying out the money for the property, labor, or services. 152

Webb, 110 Ala. 214.

California: Chater v. San Francisco Sugar Refining Co., 19 Cal. 219; Kellerman v. Maier, 116 Cal. 416; Smith v. Ferries & Cliff House R. Co., 51 Pac. 710.

Colorado: Arapahoe Cattle & Land Co. v. Stevens, 13 Colo. 534.

Georgia: Hayden v. Atlanta Cot-

ton Factory, 61 Ga. 233.
Illinois: Farwell v. Great Westrn Tel. Co., 161 Ill. 522; Richwald v. Commercial Hotel Co., 106 Ill. 439; Higgins v. Lansingh, 154 Ill. 301; Coleman v. Howe, 154 Ill. 458, 45 Am. St. Rep. 133; Sprague v. National Bank of America, 172 Ill. 149, 64 Am. St. Rep. 17; Davenport v. Plano Implement Co., 70 Ill. App. 161.

Indiana: Coffin v. Ransdell, 110 Ind. 417; Bruner v. Brown, 139 Ind. 600; Ohio, Indiana & I. R. Co. Bruner v. Brown, 139 v. Cramer, 23 Ind. 490; Cincinnati, Indianapolis & C. R. Co. v. Clarkson, 7 Ind. 595.

Iowa: Osgood v. King, 42 Iowa, 478; Wishard v. Hansen, 99 Iowa, 307, 61 Am. St. Rep. 238; Jackson v. Traer, 64 Iowa, 469, 52 Am. Rep. 449; Price v. Holcomb, 89 Iowa,

Kansas: St. Louis, Ft. Scott & W. R. Co. v. Kiernan, 37 Kan. 606; Walburn v. Chenault, 43 Kan. 352.

Kentucky: Phillips v. Covington & Cincinnati Bridge Co., 2 Metc. 219; Mercer v. Park City Mineral Water Co., 18 Ky. Law Rep. 985; John R. Procter Land Co. v. Cooke, 19 Ky. Law Rep. 1734.

Louisiana: Edwards v. Bringier Sugar Extracting Co., 27 La. Ann.

Maine: Gillin v. Sawyer, 93 Me.

Maryland: Brant v. Ehlen, 59

Massachusetts: Wyman-v. American Powder Co., 8 Cush. 168; Boston, Barre & G. R. Co. v. Wellington, 113 Mass. 79; New Haven

T. R. Co., 35 Ala. 33; State v. Horse Nail Co. v. Linden Spring

Co., 142 Mass. 349. Michigan: Young v. Erie Iron Co., 65 Mich. 111; Kobogum v. Jackson Iron Co., 76 Mich. 498; Peninsular Sav. Bank of Detroit v. Black Flag Stove Polish Co., 105 Mich. 535.

Minnesota: Hastings Malting Co. v. Iron Range Brewing Co., 65 Minn. 28, 2 Smith's Cas. 831.

Missouri: Chouteau v. Dean, 7 Mo. App. 210; Liebke v. Knapp, 79 Mo. 22, 49 Am. Rep. 212, 2 Keener's Cas. 954; Garrett v. Kansas City Coal Min. Co., 113 Mo. 330, 35 Am. St. Rep. 713; Foster v. Belcher's Sugar Poffician Co., 114 Mo. er's Sugar Refining Co., 118 Mo. 238; Woolfolk v. January, 131 Mo. 620; State v. Wood, 84 Mo. 378, Nebraska: Gilkie & Anson Co.

v. Dawson Town & Gas Co., 46 Neb. 333; Troup v. Horbach, 53 Neb. 795.

New Hampshire: Libby v. Mt. Monadnock Mineral Spring & Land Co., 68 N. H. 444.

New Mexico: Medler v. Albuquerque Hotel & Opera House Co., 6 N. Mex. 331.

New York: Van Cott v. Van Brunt, 82 N. Y. 535, 2 Keener's Cas. 954; Beach v. Smith, 30 N. Y. 116; Barr v. New York, Lake Erie & W. R. Co., 125 N. Y. 263; Gamble v. Queen's County Water Co., 123 N. Y. 91, reversing 52 Hun, 166; Skinner v. Smith, 134 N. Y. 240; Beebe v. Richmond Light & Power Co., 3 App. Div. 334; American Silk Works v. Salomon, 4 Hun, 135; Powers v. Knapp, 85 Hun, 38, 158 N. Y. 733; Close v. Noye, 147 N. Y. 597.

North Carolina: Haywood Pittsborough Plank Road Co. v. Bryan, 6 Jones Law, 82; Clayton v. Ore Knob Co., 109 N. C. 385.

Ohio: Goodin v. Evans, 18 Ohio St. 150; Gates v. Tippecanoe Stone Co., 57 Ohio St. 60.

Pennsylvania: Carr v. Le Fevre, 27 Pa. St. 413; Philadelphia & The character of the property, labor, or services is altogether immaterial, except that they must be such as the corporation, under its charter, has the power to acquire and pay for. "Payment of stock subscriptions \* \* \* may be in whatever, considering the situation of the corporation, represents to that corporation a fair, just, lawful and needed equivalent for the money subscribed." <sup>153</sup>

In accordance with this doctrine, it has repeatedly been held that a corporation, if its charter requires or authorizes it to hold land, or a patent, or any other property, real or personal, may purchase the same, and issue its stock in payment therefor, or may take the same in payment of subscriptions, provided the transaction is in good faith. "In the absence of fraud," said the Massachusetts court, "an agreement may ordinarily be made by which stockholders can be allowed to pay for their shares in patents, mines, or other property, to which it is not easy to assign a determinate value." 154 It has often been

West Chester R. Co. v. Hickman, 28 Pa. St. 318; Shannon v. Stevenson, 173 Pa. St. 419; Johnston v. Markle Paper Co., 153 Pa. St. 189; American Tube & Iron Co. v. Baden Gas Co., 165 Pa. St. 489; McNeal Pipe & Foundry Co. v. Bullock, 174 Pa. St. 93.

Tennessee: Searight v. Payne, 6 Lea, 283; Bedford County v. Nashville, Chattanooga & St. L. R. Co., 14 Lea, 525; Albitztigui v. Guadalupe, etc., Min. Co., 92 Tenn. 598; Kelley Bros. v. Fletcher, 94 Tenn. 1; Jones v. Whitworth, 94 Tenn. 602; Shields v. Clifton Hill Land Co., 94 Tenn. 123, 45 Am. St. Rep. 700; Bristol Bank & Trust Co. v. Jonesboro Banking Trust Co., 101 Tenn. 545.

Texas: Cole v. Adams, 92 Tex. 171; Thayer v. Wathen, 17 Tex. Civ. App. 382.

Washington: Turner v. Bailey, 12 Wash. 634; Kroenert v. Johnston, 19 Wash. 96.

Wisconsin: Whitehill v. Jacobs,

West Chester R. Co. v. Hickman, 75 Wis. 474; Potter v. Necedah 28 Pa. St. 318; Shannon v. Steven- Lumber Co., 105 Wis. 25.

See, to the contrary, Neuse River Navigation Co. v. Commissioners of Newbern, 7 Jones Law (N. C.) 275; Henry v. Vermillion & Ashland R. Co., 17 Ohio, 187. But compare the Ohio and North Carolina cases above cited.

152 Liebke v. Knapp, 79 Mo. 22,
49 Am. Rep. 212, 2 Keener's Cas.
957; Chouteau v. Dean, 7 Mo. App.
210; Fothergill's Case, 8 Ch. App.
270; Spargo's Case, 8 Ch. App. 407,
2 Smith's Cas. 841.

153 Sherwood, J., in Liebke v.Knapp, 79 Mo. 22, 49 Am. Rep. 212,2 Keener's Cas. 957.

 $^{154}$  New Haven Horse Nail Co. v. Linden Spring Co., 142 Mass. 349.

That an invention or a patent or patent right or license to use a patented article may be taken in payment of stock, see Edwards v. Bringier Sugar-Extracting Co., 27 La. Ann. 118; Whitehill v. Jacobs, 75 Wis. 474; Humaston v. American Tel. Co., 20 Wall. (U. S.) 20;

held that a corporation formed by the members of a partnership to take its property and continue its business may take a conveyance of the partnership assets, real and personal, and issue its stock to the partners in payment therefor. 155 It has also been held that a corporation formed for the purpose of constructing a plank road may take plank for use in building its road in payment for stock; 156 that a corporation for creating and maintaining a cemetery may issue its stock in payment for the land necessary for such purpose;157 that a waterworks company or gas company may issue its stock in payment for works already constructed, or in payment of contractors for their construction; 158 that an irrigation company may issue stock in payment for its wells, ditches, etc.; 159 that a mining company may issue stock in payment of a mine or mining lands, 160 or a lease of mining lands;161 that a natural gas company may take land and gas wells for the purpose of obtaining gas; 162 that stock may be issued by a corporation in payment for the good will of a business;163 that a contract may be made, by a corporation or-

State v. Webb, 110 Ala. 214; Skinner v. Smith, 134 N. Y. 240.

But it has been held that payment for stock in an invention or patent right of no ascertained value, and which turns out to be worthless, is not a payment in money or its equivalent, and is not a good payment as against creditors. Tasker v. Wallace, 6 Daly (N. Y.) 364; National Tube Works Co. v. Gilfillan, 46 Hun (N. Y.) 248; Chisholm Bros. v. Forny, 65 Iowa, 333; Van Cleve v. Berkey, 143 Mo. 109; Maine v. Butler, 130 Mass. 196. And see post, § 392, notes 282, 283.

 155 Coffin v. Ransdell, 110 Ind.
 417; Camden v. Stuart, 144 U. S.
 104; Coleman v. Howe, 154 Ill. 458, 45 Am. St. Rep. 133. And see ante, § 112.

156 Haywood & Pittsborough Plank Road Co. v. Bryan, 6 Jones Law (N. C.) 82.

301.

158 Bruner v. Brown, 139 Ind. 600; Woolfolk v. January, 131 Mo. 620; McNeal Pipe & Foundry Co. v. Bullock, 174 Pa. St. 93; Drake v. New York Suburban Water Co., 26 App. Div. (N. Y.) 499.

159 Loud v. Pomona Land & Water Co., 153 U. S. 564, 582.

160 Carr v. Le Fevre, 27 Pa. St. 417; Phelan v. Hazard, 5 Dill. 45, Fed. Cas. No. 11,068; Foreman v. Bigelow, 4 Cliff. 508, Fed. Cas. No. 4,934; Brant v. Ehlen, 59 Md. 1; Kellerman v. Maier, 116 Cal. 416; Young v. Erie Iron Co., 65 Mich. 111; Albitztigui v. Guadalupe, etc., Min. Co., 92 Tenn. 598.

161 Young v. Erie Iron Co., 65 Mich. 111.

162 American Tube & Iron Co. v. Baden Gas Co., 165 Pa. St. 489.

163 Washburn v. National Wall-Paper Co. (C. C. A.) 81 Fed. 17; Beebe v. Hatfield, 67 Mo. App. 609. 157 Higgins v. Lansingh, 154 Ill. Compare Camden v. Stuart, 144 U. S. 104.

ganized to build and maintain a bridge, with the proprietor of a newspaper, to give him stock in payment for publishing articles advertising the enterprise, and showing its value as an investment: 164 that a corporation finding it necessary to borrow money for the purposes of its business may issue stock in payment for services in procuring a loan for it;165 that a corporation may contract to issue stock as part payment for the services of a superintendent; 166 or for services of an agent in procuring subscriptions to its capital stock; 167 that a corporation may issue stock to a person in consideration of his giving up a position with another person or company, and becoming its president or manager;168 and that a corporation owning property on which there is a mortgage securing bonds issued by its predecessor may purchase the bonds, and issue its stock in payment therefor. 169

A manufacturing corporation may take an assignment of a lease in payment for stock, under the New York statute allowing property to be taken in payment.\*

A railroad company may contract to issue stock, and issue the same in payment for materials and labor in the construction of its road, or in payment of its contractors, 170 or in payment for land necessary for the construction of its road, 171 or

49 Am. Rep. 212, 2 Keener's Cas.

165 Arapahoe Cattle & Land Co. v. Stevens, 13 Colo. 534.

166 Chater v. San Francisco Sugar Refining Co., 19 Cal. 219, where it was held that performance of the services (the agreement being for a term of years) was not a condition precedent to the right to the stock.

167 Cincinnati, Indianapolis & C. R. Co. v. Clarkson, 7 Ind. 595.

168 Shannon v. Stevenson, 173 Pa. St. 419.

169 Beebe v. Richmond Light, Heat & Power Co., 3 App. Div. (N. Y.) 334.

\*Close v. Noye, 147 N. Y. 597.

170 Branch v. Jesup, 106 U. S. 468; Coe v. East & West R. Co., 52

164 Liebke v. Knapp, 79 Mo. 22, Fed. 531, affirmed in Grant v. Am. Rep. 212, 2 Keener's Cas. East & West R. Co., 54 Fed. 569, 13 & N. R. Co., 53 Fed. 889; Barr v. New York, Lake Erie & W. R. Co., 125 N. Y. 263; Ohio, Indiana & I. R. Co. v. Cramer, 23 Ind. 490; Philadelphia & West Chester R. Co. v. Hickman, 28 Pa. St. 318; Van Cott v. Van Brunt, 82 N. Y. 535, 2 Keener's Cas. 954; McMahon v. New York & Erie R. Co., 20 N. Y. 463; Peoria & Springfield R. Co. v. Thompson, 103 Ill. 187; Boody v. Rutland & Burlington R. Co., 24 Vt. 660; Jackson v. Traer, 64 Iowa, 469, 52 Am. Rep. 449.

> 171 Clark v. Farrington, 11 Wis. 306, 327; Cincinnati, Indianapolis & C. R. Co. v. Clarkson, 7 Ind. 595; St. Louis, Ft. Scott & W. R. Co. v. Tiernan, 37 Kan. 606.

of damages to land caused by construction of the road. 172 "The right of the officers of a railroad corporation to enter into an agreement to build its road and pay for the construction of the same in stock or bonds, cannot be seriously questioned."173 railroad company may purchase a railroad already constructed, and issue its stock in payment, if the other company has the power to sell.174

There may be circumstances under which a corporation will have the power to issue shares of its stock for the purpose of aiding another enterprise. Thus, where an improvement company was organized to buy and sell lands, erect, sell, and lease buildings, grade and improve streets, furnish gas, electric light, and waterworks, construct and operate street railroads, furnaces, and mills, and to acquire by purchase or subscription the stock or bonds of any mining, manufacturing, water, gas, street railway, or other improvement company, it was held that it had power to issue part of its stock to a railroad company to enable it to complete its line to the property which it owned. 175

A corporation cannot, at least as against creditors or dissenting stockholders, issue its stock to a person as a gift for his influence and recommendation. 176

When a person enters into a contract with a corporation to convey property to it or perform services, and take stock in payment, or to take stock in payment of a claim which he has against it, he must take the stock at its par value, unless there is some agreement to the contrary, although it may be worth less than par.177

R. Co., 157 Pa. St. 174.

<sup>173</sup> Van Cott v. Van Brunt, 82 N. Y. 535, 2 Keener's Cas. 954.

<sup>174</sup> Branch v. Jesup, 106 U. S. 468; Grant v. East & West R. Co., 468; Grant v. East & West R. Co., 176 Peninsular Sav. Bank of De13 U. S. App. 1, 54 Fed. 569, affirm
ing 52 Fed. 531; Sprague v. National Bank of America, 172 III.
149, 45 Am. St. Rep. 17; Com. v.
Central Passenger R. Co., 52 Pa. St.
506; St. Louis, Ft. Scott & W. R.
Co. v. Tiernan, 37 Kan. 606; Smith

<sup>172</sup> Hoffman v. Bloomsburg & S. v. Ferries & Cliff House R. Co. (Cal.) 51 Pac. 710.

<sup>175</sup> McGeorge v. Big Stone Gap Imp. Co., 57 Fed. 262. As to this, see ante, § 159(d).

<sup>176</sup> Peninsular Sav. Bank of De-

The power of a corporation to issue stock at less than its par value, and the effect of overvaluation of property, labor, or services taken in payment of stock, is considered in subsequent sections.<sup>178</sup>

(b) Charter, statutory, or constitutional prohibition.—In many jurisdictions, as we shall see in another place, payment for stock in property, labor, or services is regulated by express statutory or constitutional provisions, for the purpose of preventing the issue of watered stock, 179 and it may be altogether prohibited. By the weight of authority, however, it is not prohibited by a provision that stock shall not be issued except upon payment in full, or payment of the par value, or payment in cash. 180 a man contracts to take shares under such a statute, said Lord Justice Gifford in an English case, "he must pay for them, to use a homely phrase, 'in meal or in malt;' he must either pay in money or in money's worth. If he pays in one or the other, that will be a satisfaction." 181 This conclusion, it has been said in substance, "rests upon the common-sense idea that the statute does not exact of the company the barren form, the idle ceremony, of taking a check from the shareholder for the value of his stock with one hand, and giving him simultaneously with the other a check for the same amount for the property which it is authorized to purchase from him."182

Where a statute provides that subscriptions to the capital stock of a corporation "must be payable in money," a subscription by which it is agreed that land shall be conveyed to the corporation in payment is prohibited and unenforceable. 183

The fact that a corporation, because of charter or statutory

stock at its par value. Hoffman v. Bloomsburg & Sullivan R. Co., 157 Pa. St. 174.

178 See post, §§ 390(b), 391, 392,

179 See post, § 391 et seq.

180 Drummond's Case, 4 Ch. App.
772; Spargo's Case, 8 Ch. App. 407,
2 Smith's Cas. 841; Coates' Case, L.
R. 17 Eq. 169; Liebke v. Knapp, 79
Mo. 22, 49 Am. Rep. 212, 2 Keener's

182 Sherwood,
Knapp, 79 Mo. 2
2 Keener's Cas.

188 Knox v. Co., 86 Ala. 180.

Cas. 957; In re Wragg [1897] 1 Ch. 796; Larocque v. Beauchemin [1897] App. Cas. 358.

181 Drummond's Case, 4 Ch. App.

182 Sherwood, J., in Liebke v.
 Knapp, 79 Mo. 22, 49 Am. Rep. 212,
 Keener's Cas. 957.

188 Knox v. Childersburg Land Co., 86 Ala. 180.

provisions, has no power to receive subscriptions payable in property or services, as where subscriptions are required to be payable in cash, does not prevent the corporation, after it is formed, from accepting payment in property or services needed in its business, if the transaction is free from fraud, and the value of the property or services is such as to make them a fair equivalent of cash.184

(c) Ultra vires transactions.—A corporation, of course, cannot lawfully issue stock for property, labor, or services which its charter does not authorize it to acquire, or for property, labor, or services acquired for an unauthorized purpose. And it has been held that persons who take the stock under such circumstances, and transfer the property to the corporation in payment, are liable on the stock as not being fully paid up. 185 Where a manufacturing corporation organized for the manufacture of electric lamp appliances and other articles connected with electric machinery issued stock to individuals in exchange for an assignment from them to it of a contract with a foreign corporation, by which they had acquired the exclusive right to sell its product in the state and elsewhere, it was held that the contract was ultra vires, as the business proposed to be carried on under it was foreign to the business for which the corporation was created, and that the purchase of the contract was not a purchase of property necessary to its business, within a statute allowing such a purchase, and payment of the price in stock, and exempting the holders from liability to any further payments.186

lington, 113 Mass. 79.

185 Powell v. Murray, 3 App. Div. (N. Y.) 274, 157 N. Y. 717.

(N. Y.) 273, 157 N. Y. 717.

184 Frenkel v. Hudson, 82 Ala. in business in territory outside the 158, 60 Am. Rep. 736; Knox v. Chilterritory to which it is restricted dersburg Land Co., 86 Ala. 180; by its articles of incorporation, at Coe v. East & West R. Co., 52 Fed. least without the consent of all the 531; Beach v. Smith, 30 N. Y. 116; stockholders. Kimball v. New Boston, Barre & G. R. Co. v. Wel- England Roller Grate Co., 69 N. H. 485.

A corporation for the purpose of manufacturing and supplying elec-18e Powell v. Murray, 3 App. Div. tricity for lighting, heating, and v. Y.) 273, 157 N. Y. 717. power cannot issue its stock for A corporation cannot issue stock electric light plants acquired for for a patent to enable it to engage the purpose of sale. Montgomery

(d) Questions elsewhere treated.—Many questions relating to the payment or agreement to pay for stock in property, labor, or services will be considered in subsequent sections,—as the questions whether stock so paid for is watered or fictitiously paid up, and the rights and liabilities of the parties when it is so;187 whether subscriptions so payable can be received and counted in determining whether the required amount of stock has been subscribed; 188 whether agents of a corporation or commissioners have authority to receive subscriptions so payable, and the effect of their not having such authority;189 whether parol evidence is admissible to show that subscriptions are so payable; 190 and the construction of subscriptions. 191

## Payment in notes, bonds, mortgages, etc.

If subscriptions are not yet due, or if the corporation has the power to extend the time of payment, and there is no charter or statutory prohibition, it may lawfully take the subscribers' or a third person's notes or bonds in payment, payable either on demand or at a fixed time in the future. 192 It may take a note

v. Brush Electric Illuminating Co., 48 App. Div. (N. Y.) 12, affirmed 168 N. Y., mem.

The prohibition in the New York stock corporation law against the issue of stock by a corporation, except for property actually received for its "lawful purposes," does not restrict a corporation, organized to manufacture, sell, and distribute of another gas company, if the transaction is otherwise permissi-Co. 37 App. Div. (N. Y.) 618. 187 Post, § 389 et seq.

- 198 Post, § 503 et seq.
- 140 Post, § 450. 190 Post, 8 467(e).
- 171 Post. 8 465 et seq.

192 Goodrich v. Reynolds, 31 Ill. 542; Clark v. Farrington, 11 Wis. prevent it from afterwards selling

306; Blunt v. Walker, 11 Wis. 334, 78 Am. Dec. 709; Pacific Trust Co. v. Dorsey, 72 Cal. 55; Valk v. Crandall, 1 Sandf. Ch. (N. Y.) 179; Magee v. Badger, 30 Barb. (N. Y.) 246; Protection Life Ins. Co. v. Oscood. 22 Ill. 69. Chettein v. Berned. good, 93 Ill. 69; Chetlain v. Republic Life Ins. Co., 86 Ill. 220; Vermont Central R. Co. v. Clayes, 21 Vt. 30; Southern Life Ins. & Trust Co. v. Lanier, 5 Fla. 110, 58 gas, exclusively to the object thus Trust Co. v. Lanier, 5 Fla. 110, 58 expressed; but it may issue its Am. Dec. 448; Rouse, Hazard & stock in exchange for all the stock Co. v. Detroit Cycle Co., 111 Mich. 251; Merrill v. Reaver, 50 Iowa, 404; Henderson & Nashville R. Co. ble. Rafferty v. Buffalo City Gas v. Moss, 2 Duv. (Ky.) 242; Lewis v. Robertson, 13 Smedes & M. (Miss.) 558; Bates v. Lewis, 3 Ohio St. 459; Union Central Life Ins. Co. v. Curtis, 35 Ohio St. 343; Lyon v. Ewings, 17 Wis. 61; Andrews v. Hart, 17 Wis. 297.

A charter provision requiring a 490, 83 Am. Dec. 240; Stoddard v. corporation to take securities for Shetucket Foundry Co., 34 Conn. stock to a certain amount does not or bond secured by a mortgage on real or personal property. 193 When the charter of a corporation authorizes it to reissue surrendered stock, and invest the proceeds in bonds and mortgages, it may sell the stock directly for bonds and mortgages. 194

The fact that securities given by a party to a corporation in payment for a subscription to its capital stock prove valueless does not render the transaction fraudulent, or invalidate the certificates of stock issued and delivered, as against the corporation, when it does not appear that the party knew the securities to be valueless, or represented them to be good, or resorted to any means to mislead, deceive, or defraud the company, or prevent it from inquiring into the facts. 195 It has been held, however, that creditors of a corporation, or a receiver for their benefit, may compel a subscriber to pay in money, if the note of a third person given by him in payment is worthless, and was so when given in payment. 196

If a sale of stock by a corporation is otherwise valid, it is not vitiated by the fact that the motive of some of the directors and the purchaser was to enable the latter to vote on the stock in a certain manner at an approaching election of directors. 197

stock on other terms, or for other may invest its funds in bonds and

stock on other terms, or for other may livest its funds in bonds and securities. Utpon v. Hansbrough, 3
Biss. 417, Fed. Cas. No. 16,801.

193 Clark v. Farrington, 11 Wis. 334, tual Ins. Co., 10 N. J. Eq. 480, 64
78 Am. Dec. 709; Western Bank of Scotland v. Tallman, 17 Wis. 530; Protection Life Ins. Co. v. Osgood, 93 Ill. 69. Protection Life Ins. Co. v. Osgood, 93 Ill. 69; Southern Life Ins. & Trust Co. v. Lanier, 5 Fla. 110, 58 Am. Dec. 448; Valk v. Crandall, 1 Sandf. Ch. (N. Y.) 179; Lyon v. Ewings, 17 Wis. 61; Andrews v. Hart, 17 Wis. 297; Union Central Life Ins. Co. v. Curtis, 35 Ohio St. 242 Sec. 2012, \$187

business, and that the corporation 3 Ohio St. 459.

196 Bouton v. Dement, 123 III.

197 State v. Smith, 48 Vt. 266. A note given for stock subscribed for is not invalid because there was no intention to pay it, but it was taken merely for the purpose Life Ins. Co. v. Catalon,

343. See ante, § 187.

194 Southern Life Ins. & Trust stock was greater than it really

Co. v. Lanier, 5 Fla. 110, 58 Am. was, or preventing the predominance of certain stockholders, and Where a charter provides that these facts constitute no defense in the entire capital stock shall be an action on the note by the trustee paid in before commencement of of the corporation. Bates v. Lewis,

Payment for stock in notes or bonds may be expressly prohibited by charter or statutory provisions, as by a provision expressly requiring payment in cash. 198 When a corporation takes a note in payment of a subscription for stock in violation of a statute providing that only money, labor done, or property actually received shall be accepted in payment, or of a statute prohibiting payment otherwise than in cash, the note is not necessarily void, even in the hands of the corporation. 199 certainly is not so in the hands of a bona fide purchaser for And if the corporation procures a loan by pledge or value.200 discount of the note, the corporation cannot defeat an action to recover the loan on the ground that the taking of the note by it was prohibited, even though the lender may have had notice of the facts.201

# § 386. Issue of stock in payment of debts.

If a corporation is indebted to a subscriber or other person,

Ocoee Bank, 1 Lea (Tenn.) 398; Jefferson v. Hewitt, 103 Cal. 624.

Rountree, 7 Ala. 670; McRae v. Halsey, 109 Ala. 196; Jefferson v. Rountree, 7 Ala. 670; McRae v. Hewitt, 103 Cal. 624, as to which Russel, 12 Ired. (N. C.) 224; Greenville & Columbia R. Co. v. Woodsides, 5 Rich. L. (S. C.) 1475 199 Franklin v. Twogood, 18 Iowa, Bank v. Jenks, 7 Metc. (Mass.) 592; Pacific Trust Co. v. Dorsey, 72 Cal.

Compare, however, Hayne Beauchamp, 5 Smedes & M. (Miss.) 515; Boyd v. Peach Bottom Ry. Co., 90 Pa. St. 169.

Where a note is given by a subscriber for stock in payment of the first assessment, and a certificate of stock is thereupon issued to him, statutory or constitutional provi-sion that no corporation shall issue stock except for money paid,

198 See Alabama Nat. Bank v. labor done, or property actually re-Halsey, 199 Ala. 196; Moses v. ceived, and that all fictitious increase of stock shall be void. Pacific Trust Co. v. Dorsey, 72 Cal. 55. Compare Alabama Nat. Bank v.

sides, 5 Rich. L. (S. C.) 145, 55 for stock void because a statute Am. Dec. 708; McLaren v. Penning- makes it a misdemeanor for directton, 1 Paige (N. Y.) 102; Canal ors to receive notes in payment of Bank v. Holland, 5 La. Ann. 363; installments actually called; or be-Finnell v. Sandford, 17 B. Mon. cause a statute requires corpora-(Ky.) 748; Farmers' & Mechanics' tions to publish semiannual statements of their paid-up capital, and provides that nothing shall counted as capital except money. Pacific Trust Co. v. Dorsey, 72 Cal.

A note given for additional stock after the organization of a corporation is not invalid under a statute providing that "no note given by a stockholder shall be payment of any part of the capital stock." the note is not void because of a Hacker v. National Oil Refining

200 See ante, § 217.

201 First Nat. Bank of Baldwins-

and conflicting rights of creditors are not involved, it may lawfully pay the debt by cancelling the subscription or issuing its stock.202

# Pledge of stock by corporation.

It was held in a California case that a railroad company, the charter of which provided for the issue of certificates of stock when it should be fully paid for, and which had unissued stock, could not legally issue certificates to a creditor, or to a trustee for a creditor, as collateral security, 203 but the soundness of this decision is doubtful, to say the least. However that may be, it is well settled that a corporation having unissued stock in its treasury may lawfully pledge the same as security for a debt previously contracted, or as security for a loan made to it, or a debt otherwise contracted at the time, unless it is expressly prohibited from doing so by some charter or statutory provision; and it has been held that a pledge of unissued stock is not prohibited by a constitutional or statutory provision that no corporation shall issue stock except for labor done, services performed, or money or property actually received, and that all fictitious increase of stock shall be void.<sup>204</sup> In case of default.

Ch. 200; Larocque v. Beauchemin Ch. 230; Larocque v. Beauchemin [1897] App. Cas. 358; Richardson v. Graham, 45 W. Va. 134; Libby v. Mt. Monadnock Mineral Spring & Land Co., 68 N. H. 444; Goodwin v. McGehee, 15 A'a. 232; Lohman v. New York & Erie R. Co., 2 Sandf. (N. Y.) 39; Reed v. Hoyt, 19 Jones & S. 121, 109 N. Y. 659. See post,

This satisfies a statute requiring payment "in cash." Larocque v. Beauchemin [1897] App. Cas. 358.

203 Brewster v. Hartley, 37 Cal.

15, 99 Am. Dec. 237.

204 Burgess v. Seligman, 107 U. S. 20; Union Savings Ass'n v. Seligman, 92 Mo. 635, 1 Am. St. Rep. 776; Matthews v. Albert, 24 Md. violation of such a provision. 527; Kinsman v. Fisk, 83 Hun (N.

ville v. Cornell, 8 App. Div. (N. Y.) Y.) 494; Peterborough R. Co. v. 427. Nashua & L. R. Co., 59 N. H. 385; 262 Appleyard's Case, 49 L. J. Powell v. Blair, 133 Pa. St. 550; Combination Trust Co. v. Weed, 2 Fed. 24; Gasquet v. Crescent City Brewing Co., 49 Fed. 496; Atlan-tic Trust Co. v. Woodbridge Canal & Irrigation Co., 79 Fed. 842; Par-berry v. Woodson Sheep Co., 18 Mont. 317; Bloomenthal v. Ford, [1897] App. Cas. 156, reversing [1896] 2 Ch. 525. And see Illinois Trust & Sav. Bank v. Pacific R. Co., 117 Cal. 332; Nelson v. Hubbard, 96 Ala. 238.

Compare, however, Farmers' Loan & Trust Co. v. San Diego Street Car Co., 45 Fed. 518, wherein Judge Ross held that a pledge of bonds as collateral security for a pre-existing indebtedness was in

Where stock was issued on the

the pledgee may sell the stock for what it will bring, although it may be less than par, and although the charter of the corporation may prohibit it from issuing its stock at less than par.205

The liability of the pledgee to creditors of the corporation as a stockholder is considered in a subsequent chapter.<sup>206</sup>

## § 388. Right of stockholders to preference on issue of stock.

As we shall see in a subsequent section, when a corporation increases its capital stock under authority from the legislature, stockholders at the time are entitled, in preference to others, to subscribe for or purchase the new stock in proportion to their shares of the original stock.<sup>207</sup> This rule, however, is limited to an increase of stock, and, in the absence of some express charter or statutory provision, a stockholder has no greater or different right than a stranger to subscribe for or purchase undisposed-of shares of the original stock.<sup>208</sup> And the rule does not apply where a corporation has reacquired shares of its original stock by forfeiture for nonpayment of assessments, by compromise with stockholders, or by a valid purchase, and reissues the same. Such shares are assets of the corporation, and may be disposed of by it either to stockholders or to strangers, as it may deem best.209

The unissued stock of a corporation, however, although part of the original stock, is held in trust for the stockholders in such a sense that it must be disposed of for the equal benefit of all. In disposing of it, the directors or majority of the stockholders cannot discriminate between the stockholders, or issue it to

vote of the directors, and used by Nashua & L. R. Co., 59 N. H. 385; it was held that the corporation was estopped from objecting that the issue of stock not paid up was prohibited by the constitution, and that the holder was entitled to the explaining and reversing [1896] 2 Ch. 525.

them as a pledge to obtain a loan, Atlantic Trust Co. v. Woodbridge Canal & Irrigation Co., 79 Fed. 842.

206 Post, chapter xxv.

207 Post. § 408. 208 Curry v. Scott, 54 Pa. St. 270, distinguishing same to the extent of the loan. Reese v. Bank of Montgomery Co., Gasquet v. Crescent City Brewing 31 Pa. St. 78, 72 Am. Dec. 726. See Co., 49 Fed. 496. And see Bloomsims v. Street Railroad Co., 37 enthal v. Ford, [1897] App. Cas. 156, Ohio St. 556; Brown v. Florida reversing [1896] 2 Ch. 525.

205 Peterborough R. Co. v. 209 State v. Smith, 48 Vt. 266. themselves, or to their nominees, either for the purpose of making a profit for themselves out of the transaction, or for the purpose of obtaining or retaining control of the corporation. they attempt to do so, they commit a fraud upon the other stockholders, against which a court of equity will grant relief,210 unless the right to relief is barred by laches or acquiescence.211 Or if the wrong consists in issuing the stock to some of the stockholders, to the exclusion of others, who were ready and offered to take their proportion of the shares, they may maintain assumpsit against the corporation to recover damages for breach of the contract implied from its duty to them.<sup>212</sup>

### III. WATERED OR FICTITIOUSLY PAID UP STOCK.

- In general.-By the great weight of authority, in the absence of express charter, statutory, or constitutional provisions establishing a different rule, an issue of watered or fictitiously paid up stock by a corporation, whether the issue was at a discount of its par value, or for property, labor, or services taken at an intentional overvaluation, or gratuitous, is binding upon the corporation, and as against all other parties, except in so far as it may constitute a violation of the rights of existing stockholders, or operate as a fraud upon subsequent subscribers for stock, or subsequent creditors of the corporation. To go more into detail:
- (1) The transaction or agreement cannot be attacked or repudiated by the corporation itself.
- (2) It cannot be attacked by the other parties thereto,—that is, the subscribers for or purchasers of the watered or fictitiously paid up stock.

Co., 31 Pa. St. 78, 72 Am. Dec. 726; Morris v. Stevens, 178 Pa. St. 563; Arkansas Valley Agricultural Soc. all the stockholders who were not v. Eichholtz, 45 Kan. 164. See, in arrear on the shares already also, Hilles v. Parrish, 14 N. J. Eq. taken by them, and excluding 380. Compare Brown v. Florida those who were in arrear, was an Southern Ry. Co., 19 Fla. 472.

211 St. Croix Lumber Co. v. Mittlestadt, 43 Minn. 91; Shellenberger v. Patterson, 168 Pa. St. 30; Keeney v. Converse, 99 Mich. 316.

Co., 31 Pa. St. 78, 72 Am. Dec. 726, 726. See post, § 208.

210 Reese v. Bank of Montgomery it was held that a resolution of the directors of a corporation, distributing unissued stock among unlawful imposition of a penalty on those in arrear, and a violation of the equal rights of the stockholders excluded.

212 Reese v. Bank of Montgom-In Reese v. Bank of Montgomery ery Co., 31 Pa. St. 78, 72 Am. Dec.

- (3) It cannot be attacked by other stockholders who participated, consented, or acquiesced.
  - (4) It may be attacked by dissenting stockholders.
- (5) It cannot be attacked by subsequent transferees of stock, if the transferrers could not attack it.
  - (6) The transaction, or, rather, the agreement that payment in full at the par value shall not be required, is a fraud upon subsequent creditors who deal with the corporation on the faith of its capital stock being full-paid in fact; and a court of equity, or, by statute in some jurisdictions, a court of law, will, at the instance of creditors, compel the holders of such stock, or their transferees with notice, to pay up, notwithstanding their agreement with the corporation, the difference between the par value of the stock and what has been paid therefor. This does not apply, however,
    - (a) In favor of persons who were creditors at the time of the transaction, or in favor of subsequent creditors who participated therein, or who dealt with the corporation with knowledge of the facts, or who have waived the right to complain by a special contract.
    - (b) Nor does it apply as against subsequent purchasers of the stock without notice.
    - (c) Nor does it apply where the stock had been once issued, and afterwards reacquired by the corporation, so that it had a right to sell the same at the best price obtainable.
    - (d) Nor, by the weight of authority, does it apply where an embarrassed corporation increases its capital stock under legislative authority, and sells or issues the additional stock at the best price that can be obtained, although less than par, in order to pay debts or obtain money necessary to enable it to continue its business.

In most jurisdictions, when stock is issued for property, labor, or services, at an overvaluation known to be excessive, the transaction is fraudulent as against dissenting stockholders and subse-

quent bona fide creditors, and they may compel payment of the difference between the par value of the stock and the actual value of the property, labor, or services. It is otherwise, however, if the valuation was made in good faith, and the overvaluation was due to mistake or mere error of judgment.

In some jurisdictions, the rules above stated do not apply to the full extent because of special statutory or constitutional provisions. Generally, however, they apply under such provisions.

When a corporation issues stock as full-paid, this is a representation, in the absence of anything to show the contrary, that it has received from the subscribers or purchasers the full par value of the shares, in money or its equivalent, as capital upon which to conduct its operations, and from which, if necessary, to pay its debts. In such a case, persons dealing with the corporation and becoming its creditors, and persons subscribing for or purchasing other shares, have a right to assume that the corporation has received or will receive the par value of the stock. If the shares have been issued by the corporation as full-paid, when in fact it has received or agreed to receive nothing at all for them, or less than their par value, either in money, or in property or services, the shares are said to be "watered," or "fictitiously paid up," to the extent to which they have not been or are not to be paid for.

There are various ways in which watered stock may be issued. It may be issued gratuitously,—under an agreement that nothing at all shall be paid into the corporation therefor.<sup>213</sup> Or it may be issued upon payment of, or an agreement to pay, less than its par value in money, or for cash at a discount.<sup>214</sup> Or it may be issued in payment for property, labor, or services, the value of the property, labor, or services being known to be less than the par value of the shares.215 Or it may be issued

<sup>213</sup> See Christensen v. Eno, 106 N. Y. 97, 60 Am. Rep. 429, 2 Keen-401(c).

<sup>214</sup> Scovill v. Thayer, 105 U.S. 143, 2 Keener's Cas. 897, 2 Smith's 65, 1 Cum. Cas. 870; post, §§ Cas. 818; post, §§ 390(a), 401(b).

<sup>215</sup> Garrett v. Kansas City Coal Min. Co., 113 Mo. 330, 35 Am. St. er's Cas. 1240; post, §§ 390(e), Rep. 713; Elyton Land Co. v. Birmingham Warehouse & Elevator Co., 92 Ala. 407, 25 Am. St. Rep. 390(b), 392.

in the guise of a stock dividend,—that is, issued to stockholders as a dividend representing surplus profits, or an increase in the value of property, when there are not sufficient profits or a sufficient increase in values to justify it.<sup>216</sup> In all of these cases, the stock is watered to the extent that it does not represent money or its equivalent actually received or secured to the corporation as capital.

Whether a corporation can lawfully issue stock thus watered or fictitiously paid up, and the rights and liabilities arising out of such an issue of stock, or agreement therefor, will be considered in the following sections.

# § 390. Power of corporations in the absence of express charter, statutory, or constitutional provisions.

(a) Issue of stock for less than par value.—It has been said that when the amount of the capital stock of a corporation, and the par value of its shares, are fixed by its charter or the general law, or by its articles of association in pursuance thereof, the corporation has no power to issue the stock upon payment of less than its par value. This statement, however, is entirely too broad, and is not supported by authority. The writer, after a most careful investigation, has not been able to find a single case in which such a rule has been laid down, where there was no express charter, statutory, or constitutional prohibition or provision, and where no rights of dissenting stockholders or creditors were involved.

In some jurisdictions, the issue of stock for less than its par value is expressly prohibited by statute, or by a constitutional provision, and it is sometimes prohibited by the charter of a corporation.<sup>217</sup> Even in the absence of such a prohibition, the issue of stock at less than its par value, except as hereafter explained, is in violation of the rights of dissenting stockholders who have paid the par value of their shares, and for this

<sup>&</sup>lt;sup>216</sup> See post, § 523(e).

reason ultra vires as against them. 218 It is also a fraud upon other persons subscribing for or purchasing shares at their par value in reliance upon all other subscribers or purchasers paving the same. Any secret agreement, therefore, between a corporation and a subscriber for shares, under which he is to pay less than other subscribers, is void as a fraud upon the latter.<sup>219</sup> It is also a fraud upon persons who subsequently deal with the corporation and become its creditors in the belief that its authorized capital stock has been fully paid, and, as we shall see, payment of less than the par value of stock may not be full payment as against them. 220

Where, however, there is no charter, statutory, or constitutional provision requiring that stock shall be paid for at its par value, and where no rights of other stockholders are violated, and there is no fraud as against creditors, there is nothing whatever to render it either illegal or ultra vires for a corporation to issue its stock as full-paid upon payment of less than its par value. Such a transaction is perfectly valid as between the parties, if all the stockholders consent, and the corporation cannot afterwards repudiate the agreement, and compel payment of the difference between the par value of the stock and what it has agreed upon as payment in full.221

In a leading case on this point, decided in 1881 in the supreme court of the United States, a corporation organized under the laws of Kansas, where there was no express statutory or constitutional provision on the subject, issued its stock to all of its subscribers as full-paid, upon payment of less than half of its par value, and agreed with them that no further pay-

<sup>&</sup>amp; P. R. Co., 53 Barb. (N. Y.) 513. post, § 401. See post, § 397.

<sup>219</sup> See post, § 467(c).

<sup>218</sup> Fisk v. Chicago, Rock Island 537, 37 Am. Rep. 129. And see

<sup>221</sup> Scovill v. Thayer, 105 U. S. 143, 2 Keener's Cas. 897, 2 Smith's Cas. 818; Barr v. New York, Lake Erie & W. R. Co., 125 N. Y. 263; 220 Scovill v. Thayer, 105 U. S. Flynn v. Brooklyn City R. Co., 9 143, 2 Keener's Cas. 897, 2 Smith's App. Div. (N. Y.) 269. And see Cas. 818; Union Mut. Life Ins. Co. post, §§ 395, 396, 398, and cases v. Frear Stone Mfg. Co., 97 III. there cited.

ment should be required. The court held that the agreement was valid and binding as between the corporation and the stockholders, although the stockholders might be required in equity to pay such part of the difference between the par value of the stock and the amount paid as might be necessary to satisfy the claims of creditors of the corporation. "The stock held by the defendant," said the court, "was evidenced by certificates of full-paid shares. It is conceded to have been the contract between him and the company that he should never be called upon to pay any further assessments upon it. The same contract was made with all the other shareholders, and the fact was known to all. As between them and the company this was a perfectly valid agreement. It was not forbidden by the charter or by any law or public policy, and as between the company and the stockholders was just as binding as if it had been expressly authorized by the charter. If the company, for the purpose of increasing its business, had called upon the stockholders to pay up that part of their stock, which had been satisfied 'by discount' according to their contract, they could have successfully resisted such a demand. No suit could have been maintained by the company to collect the unpaid stock for such a purpose. The shares were issued as full-paid, on a fair understanding, and that bound the company."222

An examination of the English cases and some cases in this country, which are sometimes cited as against this view, will show, either that they were decided under the influence of some special statutory or constitutional provision, 223 or that the rights of nonconsenting stockholders or creditors were involved.<sup>224</sup>

# (b) Issue of stock for property, labor, or services.—The same is

utory provision in New York af- panies purchased by it. fecting the issue of stock by rail-road companies at less than par, 223 See post, § 391.

222 Scovill v. Thayer, 105 U. S. it was not contrary to public pol-143, 2 Smith's Cas. 818, 2 Keener's icy, or otherwise illegal, for a Cas. 897, opinion by Mr. Justice railroad company with a capital stock of thirty million dollars to In Flynn v. Brooklyn City R. issue the same at fifteen cents on Co., 9 App. Div. (N. Y.) 269, it is sue the same at fifteen cents on the dollar in payment of the shares was held that, as there was no stat- of stock in other railroad com-

224 See post, §§ 397, 401.

true when a corporation issues its stock for property, labor, or services, 225 whether it issues the same at less than par upon a fair valuation of the property, labor, or services, or at par upon an overvaluation. If the transaction is unaffected by charter, statutory, or constitutional provisions, and all the stockholders consent, and the rights of creditors are not involved, the transaction is perfectly valid and binding as between the parties. As between them, the courts will treat the stock as fullpaid, in accordance with their agreement, however much the par value of the stock may exceed the value of the property, labor, or services.<sup>226</sup> "Whatever," said Judge Showalter in a federal case, "may have been in fact the value of the property turned over to the company for its stock, the company agreed to take it for the stock. The persons interested were the stockholders, and there was no dissent on the part of any person concerned from what was then done. Neither any person then holding stock, nor any person who afterwards became a stockholder by assignment from one who then held stock, can now make complaint, on behalf of the corporation, as against the fairness of that transaction. This I take to be the settled law on that subject."227

According to the weight of authority, as we shall hereafter see, such payment for the stock will not be good as against subsequent bona fide creditors of the corporation, who deal with it on the faith of its stock being fully paid, if the overvaluation of the property was fraudulent, or if it was intentional, although without any actual fraudulent intent. 228

(c) Issue of stock gratuitously.—For a corporation to issue its stock as a gratuity violates the rights of existing stockholders

125 N. Y. 263. And see post, §§ 395, 401(j).

<sup>225</sup> Ante, § 384. 226 Northern Trust Co. v. Columbia Straw Paper Co., 75 Fed. 936, affirmed, Dickerman v. Northern bia Straw Paper Co., 75 Fed. 936, Trust Co. (C. C. A.) 80 Fed. 450; affirmed Dickerman v. Northern Whitehill v. Jacobs, 75 Wis. 474; Trust Co. (C. C. A.) 80 Fed. 450. 535, 2 Keener's Cas. 954; Barr v. cases there cited. New York, Lake Erie & W. R. Co., 228 Post, § 401.

Van Cott v. Van Brunt, 82 N. Y. And see post, §§ 395, 401(j), and

who do not consent, and is a fraud upon subsequent subscribers, and upon subsequent creditors who deal with it on the faith of its capital stock. The former may sue to enjoin the issue of the stock, or to cancel it if it has been issued, and has not reached the hands of a bona fide purchaser; 229 and the latter, according to the weight of authority, may compel payment by the person to whom it was issued, to such extent as may be necessary for the payment of their claims. 230

The issue of the stock, however, or at least the agreement not to require payment, is binding as between the corporation and the other party, unless it is in violation of some charter, statutory, or constitutional provision, and the corporation cannot repudiate the agreement and compel payment therefor.<sup>231</sup> a New York case, decided in 1887, stock and bonds were issued to its stockholders by a corporation, and forty per cent. of the nominal amount of the shares was credited thereon as a gratuity, because the stockholders had been called upon to pay calls upon their original subscriptions in excess of what was expected and what was represented would be necessary at the commencement of the enterprise. It was held, there being no express statutory prohibition, that a judgment creditor of the corporation, in asserting a claim against the stockholders on account of the stock so issued, could not stand upon any right existing in the corporation itself to proceed against them. Judge Andrews said in substance: "It is very plain, upon the facts, that the plaintiff, in asserting this claim, cannot stand upon any right existing in the corporation itself to proceed against the defendant. The transactions by which he acquired the shares as paid-up shares to the extent of forty per cent. of their nominal amount, and received the bonds, created no obligation as between him and the company to pay the amount unpaid on the stock or to

Post, § 397.
 Handley v. Stutz, 139 U. S.
 230 Handley v. Stutz, 139 U. S.
 2 Keener's Cas. 976, 2 Smith's Cas. 844, 1 Cum. Cas. 855, 41 Fed.
 Richardson v. Green, 133 U.

Detroit v. Black Flag Stove Polish Co., 105 Mich. 535; post, § 401(d).

Cas. 844, 1 Cum. Cas. 855, 41 Fed. 231 Christensen v. Eno, 106 N. Y. 531; Richardson v. Green, 133 U. 97, 60 Am. Rep. 429, 2 Keener's S. 30; Peninsular Sav. Bank of Cas. 1240. And see post, § 395.

account to the company for the bonds or their proceeds. As between the defendant and the company it was not intended that the former should be accountable to the company for the amount unpaid on the stock or for the bonds. Viewing the transactions in the light most favorable to the plaintiff, the credit on the stock and the transfer of the bonds were intended as a gratuity to the stockholders who had been called upon to pay calls upon their original subscriptions in excess of what was expected and of what was represented would be necessary at the commencement of the enterprise. There can be no doubt that as between the corporation and its stockholders these transactions were binding according to the actual intention. corporation itself would have no standing to demand that the defendant should pay the forty per cent. on the stock which it acknowledged had been paid, or that he should account for the proceeds of the bonds."232

(d) Issue of new stock on increasing capital stock.—When a corporation increases its capital stock merely for the purpose of adding to the original capital stock, to enable it to do a larger and more profitable business, the increased stock is subject to the same rules as original capital stock. In the absence of statutory or constitutional provisions, its issue for less than its par value will be binding as between the corporation and the purchasers or subscribers, but full payment may be required by subsequent bona fide creditors. 233

According to the decided weight of authority, however, when an active corporation becomes embarrassed, and increases its capital stock in order to raise money for the payment of its debts, and to enable it to continue its business, it may issue the new stock for the best price that can be obtained, although it may be below par, or it may issue the same as a bonus to induce persons to purchase its bonds, and the transaction, if in good

<sup>232</sup> Christensen v. Eno, 106 N. Y. 283 Handley v. Stutz, 139 U. S. 97, 60 Am. Rep. 429, 2 Keener's 417, 2 Keener's Cas. 976, 2 Smith's Cas. 1240.

Cas. 844, 1 Cum. Cas. 855. See post, § 401(g).

faith, will be valid, not only as against the corporation itself, but also as against dissenting stockholders and subsequent bona fide creditors.234

(e) Stock issued and reacquired by corporation.—When stock is issued by a corporation for a patent or other property, a part of it is sometimes returned to the corporation as treasury stock, to be disposed of for the purpose of raising money to carry on Such stock need not be issued at par, but may its operations. be sold at the best price that can be obtained, and the purchasers will not incur liability beyond the agreed price, even to subsequent creditors.235

The same is true of stock which has been lawfully issued by a corporation, and afterwards reacquired by it by forfeiture for nonpayment of assessments thereon, or by a valid compromise or purchase. It holds such stock as it holds its other assets, and may lawfully sell the same at its market price, even as against dissenting stockholders and subsequent creditors.<sup>236</sup>

(f) Payment by application of dividends or profits.—If a corpotion has surplus profits which it may lawfully pay to the stockholders as dividends, or if it has lawfully declared dividends out of surplus profits,237 it may lawfully, by agreement with the stockholders, credit the same as a payment pro tanto on their

<sup>234</sup> Handley v. Stutz, 139 U. S. ical Co., 101 Ala. 127. 417, 2 Keener's Cas. 976, 2 Smith's Cas. 844, 1 Cum. Cas. 855; Clark v. Bever, 139 U. S. 96, 2 Keener's Cas. 967; Fogg v. Blair, 139 U. S. 118; Stein v. Howard, 65 Cal. 616, 2 Keener's Cas. 963; Kellerman v. Maier, 116 Cal. 416; Dummer v. Smedley, 110 Mich. 466, 68 N. W. 260; Mathis v. Pridham, 1 Tex. Civ. App. 58.

Contra, Jackson v. Traer, 64

See, also, Peter v. Union Mfg. Co., 56 Ohio St. 181, 2 Keener's Cas. 1216.

And see post, § 401(g), where this question is further considered. <sup>235</sup> See Lake Superior Iron Co. v. Drexel, 90 N. Y. 87; Davis Bros. v. Montgomery Furnace & Chem-

Alling v. Wenzel, 133 III. 264.

236 Ramwell's Case, 50 L. J. Ch. 827; Otter v. Brevoort Petroleum Co., 50 Barb. (N. Y.) 247; Chillicothe Branch of State Bank of Ohio v. Fox, 3 Blatchf. 431, Fed. Cas. No. 2,683; Pullman v. Railway Equipment Co., 73 III. App. 313.

In an action on an agreement by a corporation to sell its own shares at less than par, where it does not appear how the company acquired the shares, it cannot be inferred in favor of the company that the stock has not been fully paid up and afterwards acquired by the company. Otter v. Brevoort Petroleum Co., 50 Barb. (N. Y.) 247.

237 Post, § 518 et seq.

subscriptions.<sup>238</sup> A corporation free from indebtedness, if acting in good faith, has the power, as between itself and its stockholders, if all consent, to agree, in consideration of the surrender by the stockholders to it of accumulated profits, and of the increased value of its property, to treat stock, upon which only fifty per cent. has been paid, as fully paid up stock; and the corporation cannot afterwards, on its own behalf, or on behalf of subsequent creditors with notice, disturb the arrangement, and compel payment of the other fifty per cent. of the stock.<sup>239</sup>

(g) Payment of commission to broker or agent.—The rule that a corporation cannot, as against dissenting stockholders or subsequent creditors, lawfully issue its stock at less than its par value, does not make it unlawful or ultra vires for a corporation to enter into a contract to pay a broker or other agent a commission for procuring subscriptions to its capital stock, or selling stock, and paying the same out of the cash received upon the subscriptions or sales.240

#### § 391. Special charter, statutory, and constitutional provisions.

The charter of particular corporations, or the general law under which they are formed, sometimes expressly provides that they shall not issue their stock for less than its par value. And in many states, to prevent the evils arising from the issue of watered or fictitiously paid up stock, and protect the public who may purchase stock or become creditors of corporations, general constitutional or statutory prohibitions have been adopted or enacted. In a number of states it is provided, in substance, that no corporation shall issue stock or bonds except for labor done or money or property actually received, and that all fictitious increase of stock or indebtedness shall be void. In

<sup>238</sup> Kenton Furnace Railroad & Mfg. Co. v. McAlpin, 5 Fed. 737; Kryger v. Andrews, 65 Mich. 405.

Whether there was fraud in such a transaction is a question for the Ass'n v. Scrimgeour, 73 L. T. 137; jury. Kryger v. Andrews, 65 Mason v. Morin, 19 Ky. Law Rep. Mich. 405.

<sup>239</sup> Kenton Furnace Railroad & Mfg. Co. v. McAlpin, 5 Fed. 737.

<sup>240</sup> Metropolitan Coal Consumers'

some, the labor or property is expressly required to be received at no greater value than the market price. There are also statutes in some states expressly prohibiting the issue of stock. whether for money or for property or labor, at less than the par value. Some of the provisions are so clear as to leave no doubt as to the intention of the legislature, while in construing others the courts have not agreed.

Construction of particular provisions.—Most of the courts, in construing the prohibitions against the issue of stock or bonds except for money or property actually received or labor done. and against fictitious increase of stock or indebtedness, hold that they were intended to protect stockholders against spoliation, and to guard the public against securities that are absolutely worthless, by preventing the flooding of the market with stock and bonds which do not represent anything whatever of substantial value; and that it was not intended to make the validity of every issue of stock or bonds by a private corporation depend upon the inquiry whether the money, property, or labor received therefor was of equal value in the market with the stock or bonds so issued, or to restrict private corporations, acting with the approval of their stockholders, in the sale or exchange of their stock or bonds for money, property, or labor, upon such terms as they may deem proper; provided, always, the transaction is a real one, based upon a present consideration, and having reference to legitimate corporate purposes, and is not a mere device to evade the law, and accomplish that which is forbidden.<sup>241</sup>

v. Dow, 120 U. S. 287, 2 Keener's 842; Brown v. Duluth, Missabe & Cas. 964; Coe v. East & West R. N. R. Co., 53 Fed. 889. See, also, Co., 52 Fed. 531; Peoria & Spring-Higgins v. Lansingh, 154 Ill. 301. field R. Co. v. Thompson, 103 Ill. Maier, 116 Cal. 416; Nelson v. least \$1,200,000, and in payment Hubbard, 96 Ala. 238; Mathis v. assumed an indebtedness of \$1,050,-

241 Memphis & Little Rock R. Co. Canal & Irrigation Co., 79 Fed.

Where a complaint alleged that 187; Stein v. Howard, 65 Cal. 616, a corporation purchased property 2 Keener's Cas. 963; Kellerman v. of another corporation worth at Pridham, 1 Tex. Civ. App. 58; Con-000, and also issued to the ventinental Trust Co. v. Toledo, St. dor's stockholders shares of stock Louis & K. C. R. Co., 82 Fed. 642; of the par value of \$2,475,000, but Atlantic Trust Co. v. Woodbridge did not allege that the purchasing

In a leading Illinois case it was said, with reference to railroad companies, that the object of such a provision "was to prevent reckless and unscrupulous speculators, under the guise or pretense of building a railroad or of accomplishing some other legitimate corporate purpose, from fraudulently issuing and putting upon the market bonds or stocks that do not, and are not intended to, represent money or property of any kind, either in possession or in expectancy, the stock or bonds in such case being entirely fictitious," and that it was not intended "to interfere with the usual and customary methods of raising funds by railroad companies for the purpose of building their roads, or of accomplishing other legitimate corporate purposes." 242

In accordance with this construction, it has been held that the prohibition against a fictitious issue of stock or bonds does not prevent a corporation from increasing its capital stock, where it has authority to do so, and selling the same at the actual market value, for the purpose of raising money needed for legitimate corporate purposes.<sup>243</sup>

A provision that "no private corporation shall issue stock or bonds except for money or property actually received, or labor done: and all fictitious increase of stock or indebtedness shall be void," does not prevent the carrying out of an agreement between the mortgage bondholders of an embarrassed railroad company, by which it is agreed that trustees shall buy in the mortgaged property on foreclosure, and convey it to a new company to be organized by the bondholders, and that the new company shall issue new mortgage bonds to pay the expenses of the sale, and other new mortgage bonds to be taken by the

corporation had any property be- Thompson, 103 III. 187, 201; Coe fore such purchase, it was held v. East & West R. Co., 52 Fed. 531; that it did not show a fictitious affirmed, Grant v. East & West R. issue of stock within the meaning Co., 13 U.S. App. 1, 54 Fed. 569. a constitutional provision against such an issue. Smith v. Ferries & Cliff House R. Co. (Cal.)

<sup>243</sup> Stein v. Howard, 65 Cal. 616, 2 Keener's Cas. 963; Kellerman v. Maier, 116 Cal. 416; Mathis v. 242 Peoria & Springfield R. Co. v. Pridham, 1 Tex. Civ. App. 58.

bondholders in lieu of their old bonds, and full paid up stock subject to the mortgage debt, to be delivered to and held by the bondholders without any payment of money.244

A provision that no corporation shall issue stock or bonds except for money paid, labor done, or property actually received, and all fictitious increase of stock or indebtedness shall be void, does not prevent a corporation from pledging its stock or bonds as collateral security for a debt less in amount than their par value.245

The good will of a business is property, and stock issued therefor is issued for property actually received, within the meaning of the constitutional and statutory provisions.246

In Alabama, there is a constitutional provision that no corporation shall issue stock except for money, labor done, or money or property actually received, and all fictitious increase of stock shall be void, and a statutory provision requiring all subscriptions to be made payable in money or in labor or property at its money value. Under these provisions it has been held that the original capital stock of a corporation, upon which it is to conduct its operations, and which must constitute the basis of its credit, cannot be lawfully issued to subscribers for less than its par value, whether it be paid for in money, or in property, labor, or services; and a fortiori, it cannot be lawfully issued gratuitously.247 Under such a prohibition, it was held illegal for a corporation to agree to issue to subscribers "five dollars of stock for one of subscription," 248 or to issue two hundred and fifty thousand dollars of stock to subscribers, being the whole capital stock, for property worth only five thousand dollars;249 or for a corporation with a capital stock of ten

<sup>&</sup>lt;sup>244</sup> Memphis & Little Rock R. Co. Cum. Cas. 870; Perry v. Tuskav. Dow, 120 U. S. 287, 2 Keener's loosa Cotton Seed Oil Mill Co., 93 Cas. 964.

<sup>245</sup> See ante, § 387.

<sup>&</sup>lt;sup>246</sup> Washburn v. National Wall-Paper Co. (C. C. A.) 81 Fed. 17.

<sup>247</sup> Elyton Land Co. v. Birming- v. Halsey, 109 Ala. 196; Beitman v. ham Warehouse & Elevator Co., 92 Steiner Bros., 98 Ala. 241.

Ala. 407, 25 Am. St. Rep. 65, 1 249 Elyton Land Co. v. Birming-

Ala. 364; Alabama Nat. Bank v.

Halsey, 109 Ala. 196.
<sup>248</sup> Williams v. Evans, 87 Ala. 725. See, also, Alabama Nat. Bank

thousand dollars to double the same, and distribute the new stock among the stockholders as a stock dividend, on the mere statement that its capital stock was invested in property which had since more than doubled in value, and was then worth twenty thousand dollars over and above all liabilities.<sup>250</sup>

This prohibition is also violated by a contract by which a corporation agrees to repay to a purchaser of stock in dividends an amount equal to the amount paid therefor.\*

In California, where it is provided by statute that "no corporation shall issue stock or bonds except for money paid, labor done, or property actually received, and all fictitious increase of stock or indebtedness shall be void," it has been held that where, after the issue of shares of stock sold at the highest market price, the market price becomes reduced, the corporation cannot issue additional shares to the purchasers, without any new consideration, for the purpose of equalizing the prices, so that their shares will not have cost them more than those to be subsequently sold at the reduced price.<sup>251</sup> It has also been held under this provision that a railroad company cannot issue a certificate of stock to a subscriber on payment by a note, the payment of which is conditional upon completion of the road within a certain time.<sup>252</sup> This provision, as we have seen, does not make stock illegal merely because it is issued for less than its par value. It is not fictitious if sold for its market value.253

In Colorado, there is a constitutional provision that "no corporation shall issue stocks or bonds, except for labor done, services performed, or money or property actually received, and all fictitious increase of stock or indetebdness shall be void," and this provision has been embodied in the statutes relating to corporations. Under this provision, persons to whom stock

ham Warehouse & Elevator Co., 92 Ala. 407, 25 Am. St. Rep. 65, 1 Cum. Cas. 870. And see Roman v. Dimmick, 115 Ala. 233.

<sup>250</sup> Fitzpatrick v. Dispatch Publishing Co., 83 Ala. 604. And see 624. Parsons v. Joseph, 92 Ala. 403.

<sup>\*</sup>Smith v. Alabama Fruit Growing & Winery Ass'n, 123 Ala. 538.

251 Kellerman v. Maier, 116 Cal.

 $<sup>^{252}</sup>$  Jefferson v. Hewitt, 103 Cal. 624.

<sup>&</sup>lt;sup>253</sup> Stein v. Howard, 65 Cal. 616,

is issued, without their paying or agreeing to pay anything at all, is absolutely void, and the holders do not thereby become in any sense shareholders of the corporation, so as to have a status to maintain an action as such.254

In Kentucky it is provided that "no corporation shall issue stock or bonds except for an equivalent in money paid, or labor done, or property actually received and applied to the purposes for which such corporation was created, and neither labor nor property shall be received in payment of stock or bonds at a greater value than the market price at the time the said labor was done or property delivered, and all fictitious increase of stock or indebtedness shall be void." Under this provision, it has been held that stock and bonds of a corporation cannot be issued for labor or property unless the market price thereof is equal to the par value of the stock or bonds.<sup>255</sup>

In Minnesota it is provided by statute that "corporations having capital stock divided into shares, unless specially authorized, shall not issue any shares for a less amount to be actually paid in on each share than the par value of the shares first issued;" and this prevents a corporation, without special authority, from issuing stock as full paid upon payment of less than par.256 An agreement between a corporation and subscribers for stock that, for every share paid for, two or more shares shall be issued, is illegal and void.257

this section, notes 241, 243.

254 Arkansas River L., T. & C. Co. v. Farmers' L. & T. Co., 13 Colo. 587. See post, §§ 395(b), 396.

255 Altenberg v. Grant (C. C. A.) 85 Fed. 345, distinguishing Memphis & Little Rock R. Co. v. Dow, 120 U. S. 287, 2 Keener's Cas. 964.

256 Wallace v. Carpenter Electric Heating Mfg. Co., 70 Minn. 321, 68 Am. St. Rep. 530.

Where a statute prohibits a corporation, unless expressly authorized, from issuing any shares for a less amount, to be actually paid in on each share, than the par

2 Keener's Cas. 963. See supra, value of the shares first issued, and an amendment thereof contains the same provision, but with a proviso that certain corporations "shall have power to create, issue and dispose of such an amount of special, preferred, or full-paid stock \* \* \* as may be deemed advisable by the board of directors," the proviso does not authorize such a corporation to issue stock as fully paid up, and sell it for less than par, or on such terms as its directors deem advisable. Wallace v. Carpenter Electric Heating Mfg. Co., 70 Minn. 321, 68 Am. St. Rep. 530. 257 Rogers v. Gross, 67 Minn. 224.

In Missouri, where the constitution provides that no corporation shall "issue stock or bonds except for money paid, labor done, or property actually received; and all fictitious increase of stock or indebtedness shall be void," it is held that a corporation cannot legally issue original stock for property or labor, unless the property or labor is reasonably worth the face value of the stock. And it was held, therefore, that a party to a contract by which a large amount of paid-up capital stock in a corporation, to be afterwards organized for the development of certain lands, was to be issued to him in exchange for his equitable rights in options on such lands, and for his services in promoting the corporation, could not enforce the contract, where it was apparent on the face of the instrument that his interest in the lands and his services, when taken together, were nothing like a fair equivalent for the face value of the stock.258

In Montana, the constitution provides that no corporation shall issue stock except for labor done or money or property actually received, and all fictitious increase of stock shall be void. And it is provided by statute that stockholders shall be individually liable to creditors, to the amount of their unpaid stock, for all acts of the company, until the whole amount of stock subscribed for shall have been paid in. It is also provided that the trustees of a company may purchase mines, and issue stock to the amount of the value thereof in payment, which shall be full-paid stock, and not liable to any further call. Under these provisions, the purchase of a mine which the stockholders knew to be worth only \$125,000, and payment therefor in stock whose par value was \$7,500,000, which was repurchased by the stockholders at two and one-half per cent. of its par value, was held fraudulent as to creditors, and the stock was treated as unpaid stock to the extent of the difference between the actual value of the mine and the par value of the stock.259

258 Garrett v. Kansas City Coal Rep. 713. See, also, Van Cleve v. Min. Co., 113 Mo. 330, 35 Am. St. Berkey, 143 Mo. 109.

258 Kelly v. Clark, 21 Mont. 291.

In New Hampshire, under a statute prohibiting a corporation from disposing of its shares at less than par, except in sales at auction for nonpayment of assessments, and declaring that all certificates of stock issued without full payment of the par value of the stock shall be void, it was held that certificates of shares of stock issued by a corporation upon its organization to pay promoters for certain patents, and by them transferred to one of their number to hold as treasury stock, were without consideration and void, and that a portion of such issue, reissued for less than par, was void.\*

In New York, under the provision of the act relating to manufacturing corporations, and authorizing the trustees of such a corporation to purchase property necessary for its business, and issue stock to the extent of the value thereof in payment, which stock shall be declared and taken to be full-paid stock, and not liable to any further calls, a manufacturing corporation has no power to issue its stock in payment for property purchased at less than its par value, and the property must be taken at a reasonable valuation.<sup>260</sup> Under a statute (New York) providing that the capital stock of a corporation "shall all be paid in, one-half thereof within one year, and the other half thereof within two years, from the incorporation of said company or such corporation shall be dissolved," a corporation cannot issue its original capital stock at less than its par value.<sup>261</sup>

In Pennsylvania, the constitution provides that "no corporation shall issue stock or bonds, except for money, labor done, or money or property actually received; and all fictitious increase of stock or indebtedness shall be void." And a statute provides that "no railway corporation" shall issue stock for less than its par value, which par value in money shall be actually paid into the treasury of the corporation before the stock is-

<sup>\*</sup>Kimball v. New England Roller- ter Co., 123 N. Y. 91, reversing 52 Grate Co., 69 N. H. 485. Hun, 166.

<sup>261</sup> Zelaya Min. Co. v. Meyer, 8 260 Gamble v. Queen's County Wa- N. Y. Supp. 487.

The act then provides a form of procedure by the attorney general, by which the act may be enforced, and the stock or bonds, or both, issued in violation thereof be adjudged void, and the officer or officers issuing the same punished as provided in the act. The statute applies to street railroad companies, as well as other kinds of railroad companies.262 provision that stock shall not be issued except for money, labor done, or money or property actually received, does not prevent a corporation from issuing stock for services to be thereafter performed, if the transaction is bona fide. 263

In Wisconsin, it is provided that "no corporation shall issue any stock, or certificate of stock, except in consideration of money, or labor, or property, estimated at its true money value, actually received by it, equal to the par value thereof; \* \* \* and all bonds issued contrary to the provisions of this section, and all stock dividends or other fictitious increase of the capital stock of any corporation, shall be void: provided, however, that any corporation whose stock or bonds have been or shall hereafter be admitted to the stock exchange of Chicago, New York, Boston, or Philadelphia, or of either of said cities, may sell such stock or bonds so admitted at the best price or prices current for the time being obtainable therefor," etc. And it is held under this provision that a corporation cannot issue stock to subscribers either gratuitously or at less than its par value, and that a fictitious issue of stock is void.264

In England, it is provided by a statute that "every share in any company shall be deemed and taken to have been issued and to be held subject to the payment of the whole amount thereof in cash, unless the same shall have been otherwise de-

<sup>262</sup> Cheetham v. McCormick, 178 Pa. St. 186.

<sup>263</sup> Shannon v. Stevenson, 173 Pa. St. 419.

<sup>264</sup> Clarke v. Lincoln Lumber Co., 23 Am. St. Rep. 417.

Since certificates of stock issued in violation of this prohibition are void, and can impose no liability upon the corporation, it has been held that sureties on the bond of an officer of a corporation are not 59 Wis. 655; Hinckley v. Pfister, liable to the corporation for the 83 Wis. 644. See Gogebic Inv. Co. value of stock so issued by the v. Iron Chief Min. Co., 78 Wis. 427, officer. First Avenue Land Co. v. Parker (Wis.) 86 N. W. 604.

termined by a contract duly made in writing, and filed with the registrar of joint-stock companies at or before the issue of such shares." And it is held, under this provision, that any agreement to issue shares for cash at a discount is illegal and void, in the absence of a contract in writing, and that the persons who take shares under such an agreement are liable for the par value.265

Full-paid stock returned to corporation.—Where shares of stock have been fully paid for, there is nothing whatever to prevent the stockholders from returning the whole or a part thereof to the corporation or a trustee for its use; and if they do so, the corporation or the trustee, subject to the terms upon which the stock is transferred, may sell or dispose of the same, as it may see fit, without violating constitutional or statutory provisions regulating the issue of stock.<sup>266</sup>

#### Valuation of property, labor, or services received in pay-§ 392. ment for stock.

As we have seen, in some jurisdictions there are statutory or constitutional provisions expressly requiring that property, labor, or services taken by a corporation in payment of stock shall be taken at a fair valuation. And sometimes the charter of a corporation contains such a provision.<sup>267</sup> Even in the absence of an express provision, it operates as a fraud upon dissenting stockholders,268 and upon subsequent creditors relying upon the capital stock being fully paid,269 for the corporation to issue stock for property, labor, or services taken at an overvaluation. If a corporation, therefore, fraudulently issues its stock

<sup>265</sup> In re Railway Time Tables Co., 43 Ch. Div. 118; In re Almada Pub. Co. [1895] 1 Ch. 255, 2 & Tirite Co., 38 Ch. Div. 415. Smith's Cas. 860, affirmed in Welton v. Saffery, [1897] App. Cas. 299. See, also, Ooregum Gold Min. Co. v. Roper, [1892] App. Cas. 125, 66 L. T: 427, 2 Cum. Cas. 247; In re Addlestone Linoleum Co., 37 Ch. Div. 191, 58 L. T. 428; In re London Celluloid Co., 39 Ch. Div. 190, 59 L. T. 109; In re New Eberhardt

<sup>266</sup> Davis Bros. v. Montgomery Furnace & Chemical Co., 101 Ala. 127; Pullman v. Railway Equipment Co., 73 Ill. App. 313. And

see post, § 401(h). <sup>267</sup> Ante, § 391.

<sup>268</sup> Post, § 397.

<sup>269</sup> Post, § 401.

1214

for property, labor, or services at an overvaluation, the transaction is illegal under some of the statutory or constitutional provisions referred to, and, even in the absence of such a provision, is illegal as against dissenting stockholders and subsequent bona fide creditors. 270 Their rights and remedies in such a case will be shown in subsequent sections.

270 United States: Camden v. Stuart, 144 U. S. 104; Grant v. East & West R. Cc., 13 U. S. App. 1, 54 Fed. 569; Altenberg v. Grant (C. C. A.) 85 Fed. 345; Peck v. Elliott (C. C. A.) 79 Fed. 10; Northwestern Mut. Life Ins. Co. v. Cotton Exchange Real Estate Co., 46 Fed. 22, 70 Fed. 155; New Castle Northern Ry. Co. v. Simpson, 21

Alabama: Elyton Land Co. v. Birmingham Warehouse & Elevator Co., 92 Ala. 407, 25 Am. St. Rep. 65, 1 Cum. Cas. 870.

Illinois: Coleman v. Howe, 154 Ill. 458, 45 Am. St. Rep. 133; Farwell v. Great Western Tel. Co., 161 Ill. 522; Sprague v. National Bank of America, 172 Ill. 149, 64 Am. St.

Índiana: Coffin v. Ransdell, 110 Ind. 417; Clow v. Brown, 150 Ind. 185; Bent v. Underdown, 156 Ind.

Iowa: Osgood v. King, 42 Iowa, 478; Chisholm Bros. v. Forny, 65 Iowa, 333; Boulton Carbon Co. v. Mills, 78 Iowa, 460; Stout v. Hubbell, 104 Iowa, 499; Wishard v. Hansen, 99 Iowa, 307, 61 Am. St. Rep. 238.

Maine: Libby v. Tobey, 82 Me.

397.

Maryland: Crawford v. Rohrer, 59 Md. 599.

Michigan: Young v. Erie Iron Co., 65 Mich. 111; Peninsular Sav. Bank of Detroit v. Black Flag Stove Polish Co., 105 Mich. 535.

Wallace v. Carpen-Minnesota: ter Electric Heating Mfg. Co., 70 Minn. 321, 68 Am. St. Rep. 530; Hastings Malting Co. v. Iron Range Brewing Co., 65 Minn. 28, 2 Smith's Cas. 831.

Mo. 410, qualified in Woolfolk v. January, infra; Garrett v. Kansas City Coal Min. Co., 113 Mo. 330, 35 Am. St. Rep. 713; Woolfolk v. January, 131 Mo. 620; Van Cieve v. Berkey, 143 Mo. 109.

Montana: Kelly v. Fourth of July Min. Co., 53 Pac. 959.

Nebraska: Gilkie & Anson Co. v. Dawson Town & Gas Co., 46 Neb.

New Jersey: Wetherbee v. Baker, 35 N. J. Eq. 501; Hebberd v. Southwestern Land & Cattle Co., 55 N. J. Eq. 18; Lee v. Heppenheimer, 55 N. J. Eq. 240.

New York: Gamble v. Queen's County Water Co., 123 N. Y. 91, reversing 52 Hun, 166; Herbert v. Uhl, 66 Hun, 626; National Tube Works Co. v. Gilfillan, 46 Hun, 248, 124 N. Y. 302.

North Carolina: Clayton v. Ore Knob Co., 109 N. C. 385.

Ohio: Gates v. Tippecanoe Stone Co., 57 Ohio St. 60.

Washington: Manhattan Trust Co. of New York v. Seattle Coal & Iron Co., 16 Wash. 499; Adamant Mfg. Co. of America v. Wallace, 16 Wash, 614, qualified in Kroenert v. Johnston, 19 Wash. 96.

Wisconsin: Gogebic Inv. Co. v. Iron Chief Min. Co., 78 Wis. 427, 23 Am. St. Rep. 417; National Bank of Merrill v. Illinois & Wisconsin

Lumber Co., 101 Wis. 247.

As to the admissibility of evidence, see Huntington v. Attrill, 118 N. Y. 365; White, Corbin & Co. v. Jones, 86 Hun, 57, 155 N. Y. 475; Blake v. Griswold, 103 N. Y. 429; Ferguson v. Gill, 64 Hun (N. Y.) 284; Thurber v. Thompson, 21 Hun (N. Y.) 472.

A provision in the charter of a Missouri: Shickle v. Watts, 94 corporation, that the capital stock

It has been said that "a gross and obvious overvaluation of property would be strong evidence of fraud," 271 but, according to the better opinion, it is more than this. If a gross and obvious overvaluation is unexplained, it is conclusive evidence that the overvaluation was intentional and fraudulent.<sup>272</sup> Some of the courts have held, or seem to have held, that there must be actual fraud; 273 but the weight of authority is to the effect that an actual fraudulent intent is not necessary if the overvaluation was intentional. An intentional overvaluation is fraudulent as a matter of law.274 "Where the nature and condition of the property," said the Minnesota court, "are such that its

"shall be issued as full-paid stock," does not permit shares of stock to be issued to stockholders without payment for it by them in money, or its equivalent in property at an honest valuation. Clayton v. Ore Knob Co., 109 N. C. 385. <sup>271</sup> Coit v. Gold Amalgamating Co., 119 U. S. 343, 2 Smith's Cas. 839, 1 Cum. Cas. 847, 14 Fed. 12.

272 Elyton Land Co. v. Birmingham Warehouse & Elevator Co., 92 Ala. 407, 25 Am. St. Rep. 65, 1 Cum. Cas. 870, where \$200,000 of stock was issued to subscribers for property which cost them, and which was only worth, \$5,000. See, also, Malting Co. v. Iron Range Brewing Co., 65 Minn. 28, 2 Smith's Cas. 831; Camden v. Stuart, 144 U. S. 104; Coleman v. Howe, 154 Ill. 458, 45 Am. St. Rep. 133; Douglass v. Ireland, 73 N. Y. 104; Boynton v. Andrews, 63 N. Y. 93; Boynton v. Hatch, 47 N. Y. 232; National Tube Works Co. v. Gilfillan, 124 N. Y. 302, 46 Hun, 248; Osgood v. King, 42 Iowa, 478; Chisholm Bros. v. Forny, 65 Iowa, 333; Van Cleve v. Berkey, 143 Mo. 109; Kelly v. Fourth of July Min. Co. (Mont.) 53 Pac. 959; Wetherbee v. Baker, 35 N. J. Eq. 501; Hebberd v. Southwestern Land & Cattle Co., 55 N. J. Eq. 18; Gilkie & Anson Co. v.

333; Manhattan Trust Co. of New York v. Seattle Coal & Iron Co., 16 Wash. 499.

Where increased stock of a corporation is required by the terms of the authority for the increase to be sold at par, and the corporation buys from a subscriber for the increased stock a patent of no value, for the purpose of allowing him to get his stock below par, by crediting the purchase price on his subscription, and afterwards resells the patent to him for a nominal sum, the transaction, being a mere evasion of the requirements of the statute, does not entitle the Wallace v. Carpenter Electric subscriber to any credit on his sub-Heating Mfg. Co., 70 Minn. 321, scription as against creditors, or 68 Am. St. Rep. 530; Hastings a receiver suing on their behalf. Peck v. Elliott (C. C. A.) 79 Fed.

<sup>273</sup> Coit v. Gold Amalgamating Co., 119 U. S. 343, 2 Smith's Cas. 839, 1 Cum. Cas. 847; Whitehill v. Jacobs, 75 Wis. 474; Kroenert v. Johnston, 19 Wash. 96, qualifying Adamant Mfg. Co. of America v. Wallace, 16 Wash. 614.

274 Boynton v. Andrews, 63 N. Y. 93: Lake Superior Iron Co. v. Drexel, 90 N. Y. 87; Douglass v. Ireland, 73 N. Y. 100; National Tube Works Co. v. Gilfillan, 124 N. Y. 302, 46 Hun, 248; Gates v. Tippecanoe Stone Co., 57 Ohio St. 60; Elyton Land Co. v. Birmingham Warehouse & Elevator Co., 92 Ala. Dawson Town & Gas Co., 46 Neb. 407, 25 Am. St. Rep. 65, 1 Cum.

value is well known and understood, or is capable of being readily estimated and ascertained, and the property is transferred to the corporation at a gross overvaluation for paid-up shares, the transaction is prima facie fraudulent as to subsequent creditors, and as against them the burden is upon the shareholder to rebut the presumption by clear and satisfactory evidence. If he knew or ought to have known that he was paying for his stock in property at a material overvaluation, it will not be sufficient for him to show, as a mental operation, that he did not intend to defraud any one. He must go further, and show that, in the exercise of ordinary business sense, he was justified in believing, and did honestly believe, that the property was being turned in at a fair valuation. Where the facts are undisputed, and the overvaluation so great as to show that the stockholder ought to have known it if he had exercised ordinary business prudence, his actual belief or intention in the premises will not avail him; he will be presumed to have intended the reasonable and natural consequences of his act, which is to defraud creditors in case of the insolvency of the corporation." 275

A margin, however, will always be allowed for honest differences of opinion as to value.<sup>276</sup> And, generally, the transaction will be upheld, even as against subsequent creditors, if the valuation was honestly made, although it may appear that there was an error of judgment, and that the valuation was in fact excessive.277 In other words, "the transaction may be impeached

Cas. 870; Hastings Malting Co. v. Iron Range Brewing Co., 65 Minn. 28, 2 Smith's Cas. 831; Coleman v. Smith's Cas. 831; Coleman v. Pacific Ry. Co., 66 Minn. 28, 2 Smith's Cas. 831. Smith's Cas. 840; Boulton Carbon Co. v. Mills, 78 Iowa, 460; Sprague National Bank of America, 172 Ill. 149, 64
Am. St. Rep. 17; National Bank of Co., 119 U. S. 343, 2 Smith's Cas. America v. Pacific Ry. Co., 66 Ill. 839, 2 Keener's Cas. 1887, 1 Cum. App. 320; Carp v. Chipley, 73 Mo. Cas. 847; Bank of Fort Madison v. App. 22; Kelly v. Clark, 21 Mont. Alden, 129 U. S. 372; Grant v. East 291; Manhattan Trust Co. v. Seattle Coal & Iron Co., 16 Wash. 499. Fed. 569, affirming Coe v. East & Cas. 870; Hastings Malting Co. v.

<sup>275</sup> Hastings Malting Co. v. Iron Range Brewing Co., 65 Minn. 28, 2

for fraud, but not for error of judgment or mistaken views of the value of the property, inasmuch as good faith and the exercise of an honest judgment is all that is required." 278 "Although there was in fact an overvaluation of the property, it will not render the stockholders liable for the deficiency if it was the result of an honest mistake or error of judgment." 279 This is true, even though it may turn out that the property was in fact very greatly overvalued, if it affirmatively appears that the valuation was in good faith.280

West R. Co., 52 Fed. 531; Northwestern Mut. Life Ins. Co. v. Cotton Exchange Real Estate Co., 46
Fed. 22, 70 Fed. 155; Brown v. Duluth, Missabe & N. R. Co., 53 Fed.
Hastings Malting Co. v. Iron
Range Brewing Co., 65 Minn. 28, 2
Cole v. Adams, 92 Tex. 171; Richsmith's Cas. 831; Young v. Erie
Iron Co., 65 Mich. 111; Brant v.
Ehlen. 59 Md. 1: John R. Procter

278 Douglass v. Ireland. 73 N. Y. Ehlen, 59 Md. 1; John R. Procter Land Co. v. Cooke, 19 Ky. Law Rep. 1734; Woolfolk v. January, 131 Mo. 620, overruling, to this extent, the dictum in Shickle v. Watts, 94 Mo. 410; Schenck v. Andrews, 57 N. Y. 133; Boynton v. Andrews, 63 N. Y. 93; Douglass v. Ireland, 73 N. Y. 100; Lake Superior Iron Co. v. Drexel, 90 N. Y. 77; White Centing Co. v. Drexel, 90 N. Y. 87; White, Corbin & Co. v. Jones, 86 Hun (N. Y.) 57, reversed, on other grounds, in 155 N. Y. 475; Powers v. Knapp, 85 Hun, 38, 158 N. Y. 733; Bickley v. Schlag, 46 N. J. Eq. 533; Carr v. Le Fevre, 27 Pa. St. 413; American Tube & Iron Co. v. Baden Gas Co., 165 Pa. St. 489; Kelley Bros. v. Fletcher, 94 Tenn. 1; Jones v. Whitworth, 94 Tenn. 602; Medler v. Albuquerque Hotel & Opera House Co., 6 N. M. 331; Holly Mfg. Co. v. New Chester Water Co., 48 Fed. 879; Higgins v. Lansingh, 154 Ill. 301; Gilkie & Anson Co. v. Dawson Town & Gas Co., 46 Neb. 333; Troup v. Horbach, 53 Neb. 795; Turner v. Bailey, 12 Wash. 634; Adamant Mfg. Co. of America v. Wallace, 16 Wash. 614; Kroenert v. Johnston, 19 Wash. 96.

See, also, Penfield v. Dawson

<sup>278</sup> Douglass v. Ireland, 73 N. Y. 100.

Under a New York statute prohibiting the issuing of stock of a corporation organized under it for property except for "property actually received for the use and legitimate purpose of said corpora-tion, at its fair value," the fair value of property taken by a corporation for stock is that which the property has at the time of the sale, and is not dependent upon the subsequent success or failure of the investment, further than that result may have been legitimately within evidential contemplation at the time of the sale, in view of the uses for which it may have had available advantages within itself. . Huntington v. Attrill, 118 N. Y.

279 Hastings Malting Co. v. Iron Range Brewing Co., 65 Minn. 28, 2 Smith's Cas. 831.

280 Young v. Erie Iron Co., 65 Mich. 111, and other cases above

Where the owners of land, having struck large gas wells thereon, organized a corporation, and conveyed the land to it in exchange for stock at a valuation of \$500,000, Town & Gas Co., 57 Neb. 231; Na- it was held that the fact that sub-

The fact that the property taken in payment for stock is of such a character that it is not easy to assign to it a determinate value, as in the case of patents and mines, does not necessarily render the transaction illegal, if the valuation is really made in good faith.281 But payment in a patent right or other property which has no ascertained value is not a payment in money or its equivalent, within the meaning of a statute. In such a case it was said: "The transfer of a patent which had no ascertained value; which, in the language of the witness, 'as it turned out was worth nothing,' cannot be regarded as 'money,' or its equivalent, because those engaged in the management of the company believe at the time it is valuable, and receive it after organization, upon some fixed estimate of its value, between them and the subscriber, as so much money. Before a thing can be regarded as money or its equivalent, it must have an actual, positive, and ascertained value—a value so thoroughly ascertained and fixed at the time, that it can at once be changed into money, of which it is regarded as the equivalent." 282 Indeed, it has been held that payment in an invention or patent right, or other property, which turns out to have been absolutely worthless, is not a good payment as against subsequent bona fide creditors, even where the parties believed it to be valuable. In such a case, proof of an actual fraudulent intent is not necessary to entitle such creditors to enforce payment.<sup>283</sup>

sequent operations demonstrated that the property was of very small value did not throw upon them the burden of showing that the sale to the corporation was in good faith on a reasonable belief as to the value of the property. American Tube & Iron Co. v. Baden Gas Co., 165 Pa. St. 489.

281 "In the absence of fraud, an agreement may ordinarily be made by which stockholders can be allowed to pay for their shares in buy necessary property, and issue patents, mines, or other property, full-paid stock to the amount of the to which it is not easy to assign value thereof, the directors are a determinate value." New Haven justified in refusing to issue stock

Horse Nail Co. v. Linden Spring Co., 142 Mass. 349.

<sup>282</sup> Tasker v. Wallace, 6 Daly (N. Y.) 364. See, also, National Tube Works Co. v. Gilfillan, 46 Hun (N. Y.) 248.

283 Van Cleve v. Berkey, 143 Mo.
 109, 44 S. W. 743; Chisholm Bros.
 v. Forny, 65 Iowa, 333; Henderson

v. Turngren, 9 Utah, 432. Where a statute provides that the directors of a corporation may

Where the persons conveying property to a corporation by quitclaim deed, in exchange for stock issued as full paid, have never had any title to the property, before or since, the stock is not full paid, and the subscribers are liable, at least in favor of creditors of the corporation, for the full amount of their subscriptions. It can make no difference in such a case that there was no actual fraudulent intent.284

The good-will of a business purchased by a corporation, and paid for by stock, is property, and is to be taken into consideration in determining the value paid for the stock.285

When a corporation purchases property, and issues its stock in payment, the property is properly valued at what it is actually worth, however much such value may exceed what it cost the vendor, for the cost is not the test of value. 286

for patents, in pursuance of an agreement of the corporators, where one of the patents has not been perfected, and the articles made under the other are worthless. Edgerton v. Electric Improvement & Construction Co., 50 N. J. Eq. 354.

284 Henderson v. Turngren. Utah, 432.

285 Washburn v. National Wall-Paper Co. (C. C. A.) 81 Fed. 17; Beebe v. Hatfield, 67 Mo. App. 609.

In Camden v. Stuart, 144 U. S. 104, however, where a partnership was converted into a corporation, and the property of the partners transferred to it in exchange for stock, it was held that, in ascertaining whether the stock was fullpaid as against creditors, no allowance could be made for the experience and good will of the partners, or for their trouble or loss of time, as such elements of value were too unsubstantial to be estimated for such a purpose.

<sup>286</sup> Grant v. East & West R. Co., 13 U. S. App. 1, 54 Fed. 569, af-firming Coe v. East & West R. Co., 52 Fed. 531; Com. v. Central Passenger R. Co., 52 Pa. St. 506; Dick-

ern Trust Co. v. Columbia Straw-Paper Co., 75 Fed. 936.

Under the constitutional provision in Alabama prohibiting the issue of stock or bonds except for money, labor, or property actually received, and declaring all fictitious increase of stock or indebtedness to be void, and the statutory provision requiring all subscriptions for railroad stock to be paid in money, labor, or property at its money value, railroad property sold by one company to another, and paid for in stock and bonds of the latter, may be valued according to its net earning power, and the cost of building it de novo, and it can make no difference that the seller originally acquired it for much less than its actual value. Grant v. East & West R. Co., 13 U. S. App. 1, 54 Fed. 569, affirming Coe v. East & West R. Co., 52 Fed.

Where a corporation is organized to purchase several manufacturing plants from persons holding op-tions upon them, the fact that the amounts in the stock of the corporation, at its par value, which are issued in payment of such operman v. Northern Trust Co. (C. tions, are greater than the prices C. A.) 80 Fed. 450, affirming North-fixed on the plants in the options.

A stockholder in a New York water company erected for his own use and benefit a system of pipes, etc., which were suitable for an extension to the company's plant, and sold it to the company, receiving in return stock and bonds. On the question whether there had been an overvaluation in determining the cost of construction, the court held that money saved by careful and fortunate purchase of materials, four months' interest on the actual expenditures for the work, reasonable charges for services rendered by himself and his assistant in superintending the work, and a fair profit calculated with reference to the nature and risks of the work, might be added to the money actually expended by him for materials and labor. And as it appeared that the cost of the work, calculated on such a basis, was about \$85,000, it was held that payment therefor in stock and bonds of the company of the par value of \$110,000 was not so large a price as necessarily to indicate a fraudulent overvaluation.287

Province of court and jury.—Whether or not property taken by a corporation, and paid for by the issue of stock, has been

is not evidence of overvaluation of ing the property of the corporation the plants in the sale and the issue before it was organized, the beneof the stock. Dickerman v. North- fits of which are received by it, and ern Trust Co. (C. C. A.) 80 Fed. which expenditures would have 450, affirming Northern Trust Co. been necessary if the stock had v. Columbia Straw-Paper Co., 75 been otherwise paid for, may be

<sup>287</sup> Gamble v. Queens County Water Co., 123 N. Y. 91, reversing 52 Hun, 166.

It has been held that the pro-

considered in computing the stock actually paid in, see Geneva Mineral Spring Co. v. Coursey, 45 App. Div. (N. Y.) 268.

Where the promoters of a corpovision in the New York stock cor- ration had secured a \$17,000 conporation law that no stock shall be tract for work and materials, and issued for less than its par value a valuable option contract, afterfor stock of another corporation wards exercised, which were turndoes not prohibit a gas company ed over to the company after its from purchasing all the stock of incorporation, together with land another company by issuing its of the value of \$14,000, and afterown stock therefor, merely because wards the net earnings were inthe plant and tangible property vested in the corporation, and, thus purchased are less than the some nine months thereafter, \$28,par value of the stock issued, if the 000 of stock was issued and dibenefits otherwise derived warrant vided among the promoters, it was the transaction. Rafferty v. Buf-held that, in determining whether falo City Gas Co., 37 App. Div. (N. the stock was fully paid up, the Y.) 618. value of the land, the contract, and
That payments for stock represented by expenditures in developthe issue of the stock should all be

intentionally taken at an overvaluation, and the overvaluation was fraudulent, is ordinarily a question of fact for the jury.<sup>288</sup> But, as we have seen, when it appears that property, the value of which is well known and understood, or capable of being easily ascertained, is exchanged for stock at a price which is far beyond its real value, and there is no evidence explaining the apparent bad faith, the transaction is fraudulent as a matter of law, and may be so held by the court without submitting / the question to the jury. 289

Presumption and burden of proof.—When stock has been paid for by conveyance of property to the corporation, or performance of services, and there is no evidence at all as to the value of the property or services, it will be presumed that it was adequate, and even where it appears that there was in fact overvaluation, yet, if the overvaluation was not so gross and palpable as to show that it must have been intentional, it will be presumed that the valuation was honestly made, and the burden will be upon the creditor attacking the transaction.<sup>290</sup>

tion, within the meaning of a constitutional provision as to the issue of stock. Cole v. Adams, 92 Tex. 171.

Compare Cole v. Adams, 19 Tex. Civ. App. 507.

288 Herbert v. Uhl, 66 Hun (N. Y.). 626, and other cases cited in note 270 et seq., supra.

289 Boynton v. Andrews, 63 N. Y. 93; Lake Superior Iron Co. v. Drexel, 90 N. Y. 87; Hastings Malting Co. v. Iron Range Brewing Co., 65 Minn. 28, 2 Smith's Cas. 831. And see other cases in notes 272 to 275, supra.

"Where property, whose value is well known or can be easily learned, is taken at an exaggerated estimate, a strong presumption is raised that the valuation is not in good faith and is made for a fraudulent purpose. This presumption

considered, as they were "property tory of the apparent fraud. Where actually received" by the corporative overvaluation is so great that the fraudulent intent appears on its face, and is not explained, the court will hold it to be fraudulent as matter of law." Coleman v. Howe, 154 Ill. 458, 45 Am. St. Rep.

Under a statute requiring the capital stock of a corporation to be subscribed before it can do business, a subscription for substantially all of the stock of a corporation having a capital stock of \$5,000,000, and payment thereof in undeveloped coal lands, for which the subscriber has paid \$70,000 only, is prima facie fraudulent. Manhattan Trust Co. v. Seattle Coal & Iron Co., 16 Wash. 499.

290 Davis Bros. v. Montgomery Furnace & Chemical Co., 101 Ala. 127; Carr v. Le Fevre, 27 Pa. St. 413; American Tube & Iron Co. v. Baden Gas Co., 165 Pa. St. 489; Kelley Bros. v. Fletcher, 94 Tenn. will be conclusive unless rebutted 1; Shield v. Clifton Hill Land Co., by satisfactory evidence explana- 94 Tenn. 123, 45 Am. St. Rep. 700.

## § 393. Effect of issue of, or agreement to issue, watered stock.

In the preceding sections we have considered merely the powers of corporations with respect to the issue of stock without receiving full payment, and what transactions are within particular charter, statutory, or constitutional prohibitions, and the valuation of property, labor, or services taken in payment for stock. This and the following sections will deal with the rights and liabilities arising out of the issue of watered or fictitiously paid up stock, assuming that the issue is fraudulent, ultra vires, or illegal. At the outset, it may be well to refer shortly to certain general principles which are applicable.

Rights and liabilities based upon the ground that the issue of stock or agreement is fraudulent.—Since the authorized or required capital stock of a corporation constitutes the basis of its credit, persons dealing with a corporation have a right to assume that the full amount of the stock has been actually paid in, or at least that it has been secured to be paid in, so that it will be available for the payment of the corporate debts. It follows from this that any secret arrangement between the corporation and subscribers for its capital stock, or purchasers thereof from it, to issue the stock as full-paid, when in fact it is issued gratuitously, or is to be paid for in part only, either in money, or in property, labor, or services, will operate as a fraud, not only upon persons who subsequently become creditors of the corporation on the faith of its capital stock being fully paid, but also upon other persons who may subscribe for or purchase stock of the corporation, and pay for the same in full. On equitable principles, therefore, and aside from any question as to the powers of the corporation in the absence of fraud, persons who are defrauded by such an issue of watered stock are entitled to appropriate relief in a court of equity, whether they seek such relief as creditors<sup>291</sup> or as stockhold-

<sup>291</sup> Sawyer v. Hoag, 17 Wall. (U. 458, 45 Am. St. Rep. 133; Wethers.) 610, 2 Smith's Cas. 812, 1 Cum. bee v. Baker, 35 N. J. Eq. 501; Cas. 818; Camden v. Stuart, 144 U. First Nat. Bank of Deadwood v. S. 104; Coleman v. Howe, 154 Ill. Gustin Minerva Consolidated Min.

ers.292 In such a case, a court of equity has the undoubted power to set the transaction aside so as to prevent the fraud, or relieve against it, if rights of innocent third persons have not intervened.<sup>293</sup> Or, according to the overwhelming weight of authority, it may treat the secret agreement as a nullity, and require the holders of the watered or fictitiously paid up stock to pay the full par value of the shares, so as to compel them to make good their express or implied representation that the shares are full-paid.294

Since, however, relief on the ground of fraud is not granted except to persons defrauded, no relief against an issue of watered stock can be granted, on the ground of fraud, to persons who are not defrauded thereby,—as the corporation itself,295 the state, 296 stockholders participating or becoming such with notice of the facts, 297 and transferees who stand in their shoes,298 or creditors who became such prior to the issue of the stock, or afterwards with notice, 299 etc. Their rights and remedies must be based upon some other ground than fraud. They depend upon the powers of the corporation with respect to the issue of its stock, and the effect of its exceeding its powers.

Rights and liabilities based upon the ground that the issue of stock or agreement is ultra vires .- Assuming that an agreement to issue or issue of watered or fictitiously paid up stock by a corporation is merely ultra vires or beyond its powers, and laying aside any element of fraud or illegality by reason of express charter, statutory, or constitu-

Co., 42 Minn. 327, 18 Am. St. Co., 83 Ala. 604. And see post, § Rep. 510, 2 Smith's Cas. 835, 1 397. Cum. Cas. 850. And see post, § 401.

<sup>292</sup> Melvin v. Lamar Ins. Co., 80 Ill. 446, 22 Am. Rep. 199, 2 Keener's Cas. 1197, 2 Smith's Cas. 854; Fitzpatrick v. Dispatch Publishing Co., 83 Ala. 604; Fisk v. Chicago, Rock Island & P. R. Co., 53 Barb. (N. Y.) 513. And see post, § 397. 293 Fisk v. Chicago, Rock Island

& P. R. Co., 53 Barb. (N. Y.) 513; 298 Post, \$ 399. Fitzpatrick v. Dispatch Publishing 209 Post, \$ 401(j).

<sup>294</sup> Melvin v. Lamar Ins. Co., 80 Ill. 446, 22 Am. Rep. 199, 2 Keener's Cas. 1197, 2 Smith's Cas. 852; Camden v. Stuart, 144 U. S. 104; Wetherbee v. Baker, 35 N. J. Eq. 501; and other cases in note 292, supra. See, also, post, §§ 397, 467.

<sup>&</sup>lt;sup>295</sup> Post, § 395. <sup>296</sup> Post, § 394.

<sup>&</sup>lt;sup>297</sup> Post, § 398.

tional prohibition, as shown in a former section, 300 the rights, remedies, and liabilities arising out of such an issue or agreement must be ascertained by applying the general principles in relation to ultra vires acts and contracts, which have been treated at length in a former chapter.301 In accordance with these principles, the following propositions may be laid down:

An ultra vires issue of watered or fictitiously paid up stock by a corporation may be ground for proceedings by the state to forfeit its charter for the misuser or abuse of power, although it is not necessarily so.302

Dissenting slockholders may proceed in equity to enjoin the ultra vires issue, or, subject to qualifications, to cancel the same.303 But s ockholders who participate in an ultra vires issue of stock cannot complain.304

Since an ultra vires contract which is wholly executory is void and unenforceable, a bill in equity or an action at law cannot be maintained either by or against a corporation to compel specific performance of an ultra vires contract to take or issue stock at a discount or otherwise for less than par, or to recover damages for breach thereof. 305

As we have seen, however, in an earlier chapter, an executed ultra vires contract of a corporation is not necessarily void, but, on the contrary, the general rule is that neither the corporation nor the other party to the contract can question its validity, or sue to set it aside. On general principles, therefore, where a contract for the issue of watered stock has been fully

<sup>300</sup> Ante, § 391.

<sup>301</sup> Ante, § 204 et seq. See West Cornwall Ry. Co. v. Mowatt, 12 Jur. 407; Fisk v. Chicago, Rock Islard & P. R. Co., 53 Barb. (N. Y.) 513.

<sup>302</sup> State v. Webb, 97 Ala. 111, 38 Am. St. Rep. 151; Holman v. State, 105 Ind. 569; post, § 394; ante, § 312 et seq.

<sup>303</sup> Fitzpatrick v. Dispatch Publishing Co., 83 Ala. 604; Fisk v.

Chicago, Rock Island & P. R. Co.,

<sup>304</sup> Washburn v. National Wall-Paper Co. (C. C. A.) 81 Fed. 17; Winston v. Dorsett Pipe & Paving Co., 129 Ill. 64, 2 Smith's Cas. 857. 2 Keener's Cas. 1212. And see post, § 398.

<sup>305</sup> West Cornwall Ry. Co. v. Mowatt, 12 Jur. 407; Garrett v. Kansas City Coal Min. Co., 113 Mo. 330, 35 Am. St. Rep. 713. And see post, §§ 395, 396.

executed, on both sides, by delivery of the certificates and pavment as agreed, neither the corporation nor the holders of the stock, nor participating or consenting holders of other stock. can afterwards attack the transaction merely on the ground that it was ultra vircs, there being no express prohibition or established public policy rendering the transaction absolutely null and void.307

We have also seen that, according to the weight of authority, when a contract with a corporation is merely ultra vires, not being expressly prohibited nor contrary to public policy, and has been fully executed on one side, the other party may be estopped to set up the defense of ultra vires to defeat an action against him or it on the contract.308

The mere fact that a contract or transaction on the part of a corporation is ultra vires can give strangers no right to complain; and the creditors of a corporation are strangers, at least for this purpose. The only ground upon which they can attack an issue of watered stock, assuming it to be merely voidable and not void, is that of fraud.309

Rights and liabilities based upon the ground that the issue of stock or agreement is illegal.—If a particular act or contract of a corporation is expressly prohibited by its charter or by the constitution or general statutory law, or if it violates express provisions of the law, it is, as a general rule, not merely ultra vires, but illegal; and the same is true of an act or contract which, although not expressly prohibited, is contrary to public policy. 310 An illegal contract cannot, as a rule, be enforced. follows that no action can be maintained by or against a corporation on a contract to take or issue stock which is illegal because it is contrary to an express charter, statutory, or constitutional provision, or because it is contrary to the public policy of the state.311 It is also a well-established principle that, when

<sup>307</sup> See post, §§ 395, 396, 398.

<sup>308</sup> Ante, § 214. 309 Post, § 401(a),(j). 310 Ante, § 222 et seq.

<sup>311</sup> Williams v. Evans, 87 Ala. 725; Garrett v. Kansas City Coal Min. Co., 113 Mo. 330, 35 Am. St. Rep. 713. See post, §§ 295, 396.

an illegal contract has been carried out, the courts will leave the parties where they have placed themselves, and will not entertain a suit by either party for relief from the effect of the contract. This is true of an illegal issue of stock in violation of a constitutional or statutory provision.312

If stock is issued at a discount for cash, in violation of an express statutory prohibition, the issue of the stock is not void, but the agreement that it shall be paid for at less than its par value is illegal and void, and cannot be enforced. In such a case, the subscriber or purchaser is liable for the full par value. 313

## Effect as against the state.

When a corporation is guilty of ultra vires or illegal acts which constitute an injury to or fraud upon the public, or which will tend to injure or defraud the public, the state may institute quo warranto proceedings to forfeit its charter for the misuser or abuse of its franchises.<sup>314</sup> The attorney general, therefore, may institute such proceedings to enforce a forfeiture of the charter of a corporation for an ultra vires or illegal issue of watered or fictitiously paid up stock, and the court will decree a forfeiture if the circumstances are such as to bring the case within the general principles governing the forfeiture of charters,315 as elsewhere stated and explained.316

Leave to institute such proceedings (when leave of court is

312 Clarke v. Lincoln Lumber v. Webb, 97 Ala. 111, 38 Am. St. Co., 59 Wis. 655.

313 In re Railway Time Tables Pub. Co., [1895] 1 Ch. 225, 2 Smith's Cas. 860, affirmed, Welton v. Suffery, [1897] App. Cas. 299.

814 Ante, § 312 et seq.

315 State v. New Orleans Debenture Redemption Co., 51 La. Ann. 1827; State v. Hogan (Mo.) 63 S. W. 378. And see People v. City Bank of Leadville, 7 Colo. 226; Holman should be fully paid. State v. New v. State, 105 Ind. 569; State v. Orleans Debenture Redemption Atchison & Nebraska R. Co., 24 Co., 51 La. Ann. 1827. Neb. 143, 8 Am. St. Rep. 164; State

Rep. 151.

Thus it has been held ground for forfeiture that a corporation violated a constitutional provision that no corporation should issue stock or bonds except for labor done, or money or property actually received, and a charter provision that no stock should be issued or certificate given therefor until the amount subscribed for

316 Ante, § 312 et seq.

required), or a decree of forfeiture, will be denied where there has been unreasonable delay in instituting such proceedings,<sup>317</sup> or where the state has waived the right to enforce a forfeiture,<sup>318</sup> or where the circumstances are such that the interests of the public do not require a forfeiture.<sup>319</sup>

If a threatened act of a corporation will constitute a public nuisance, and prompt action is necessary to prevent injury to the public therefrom, the attorney general, as we have seen, may proceed in equity for an injunction.<sup>320</sup> It is perhaps safe to say, however, that this principle does not authorize a suit by the attorney general to enjoin the issue of watered stock. The state cannot maintain a suit to enjoin or cancel an issue of watered or fictitiously paid up stock, where private rights only will be affected.<sup>321</sup> The state cannot maintain a suit in equity to cancel watered stock and bonds and to enjoin fore-closure of a mortgage given to secure the bonds.<sup>322</sup>

## § 395. Effect as against the corporation itself.

(a) In general.—It has been said broadly that a corporation, after issuing its stock as paid-up, and declaring it to be so,

317 State v. Janesville Water Co., 92 Wis. 496.

318 State v. Webb, 110 Ala. 214.

Where a corporation has been fraudulently organized by the corporators issuing the authorized capital stock for property worth only one-half of the par value of the stock, the legislature may by special act correct and waive the vice of the fraudulent organization by reducing the amount of the stock one-half, and cancelling the remainder of the shares, which have been surrendered to the corporation by the stockholders, and thereby purge the corporation of the fraud, and render it a de jure corporate body. State v. Webb, 110 Ala. 214.

319 State v. Minnesota Thresher Mfg. Co., 40 Minn. 213.

320 Ante, § 209.

321 State v. Farmers' Loan & Trust Co., 81 Tex. 530; Minnesota v. Guaranty Trust & Safe-Deposit Co., 73 Fed. 914.

322 Under the Minnesota statute prohibiting railroad companies from selling or disposing of any shares of stock until the same are fully paid, or issuing any stocks or bonds except for money, labor, or property actually received, and declaring all fictitious increase of stock or indebtedness void, it was held that the purpose was to protect stockholders and creditors, and that the state had no right to protect their private rights by a suit in its own name to cancel stock and bonds issued in violation of the statute, and to enjoin foreclosure of a mortgage given to secure the bonds. Minnesota v. Guaranty Trust & Safe-Deposit Co., 73 Fed. 914.

when it is not so in fact, cannot subsequently repudiate the declaration and agreement, where no actual fraud enters into the transaction, and proceed to collect, either from the person receiving the stock or his transferee, the unpaid part of the par value, as it is estopped from doing so.323 But this is not necessarily true under all circumstances. It is not true under statutory or constitutional provisions in some jurisdictions,324 and it is not always true where all the stockholders do not consent.325

It is undoubtedly true, however, as was stated in a former section, that where a corporation issues watered or fictitiously paid up stock, with the consent of all the stockholders, and when there is no charter, statutory, or constitutional provision rendering the transaction void, the agreement is valid and binding as against the corporation, and it cannot afterwards repudiate the same and exclude the holders of the stock, or compel them to pay the difference between the par value of the stock and what has been paid or agreed upon as full payment. 326 This

323 1 Cook, Corp. § 38. 324 In re Railway Time Tables Pub. Co., 71 L. T. 682; Morrow v. Nashville Iron & Steel Co., 87 Tenn. 262, 10 Am. St. Rep. 658, 2 Keener's Cas. 989. See infra, this

325 Robinson v. Pittsburgh & Connellsville R. Co., 32 Pa. St. 334; Melvin v. Lamar Ins. Co., 80 III. 446, 22 Am. Rep. 199, 2 Smith's Cas. 852, 2 Keener's Cas. 1197. See

post, §§ 397, 467(c).

326 Scovill v. Thayer, 105 U. S. 143, 2 Smith's Cas. 818, 2 Keener's Cas. 897, as to which see ante, § 390(a); Kenton Furnace R. & Mfg. Co. v. McAlpin, 5 Fed. 737; Harrison v. Union Pac. Ry. Co., 13 Fed. 522; Bruner v. Brown, 139 Ind. 600; Clow v. Brown, 150 Ind. 185; First Nat. Bank of Deadwood v. Gustin Minerva Consolidated

Keener's Cas. 1240; Callanan v.'
Windsor, 78 Iowa, 193; Whitehill
v. Jacobs, 75 Wis. 474; Hill v.
Atoka Coal & Min. Co., 124 Mo. 153.
See, also, Union Mut. Life Ins.
Co. v. Frear Stone Mfg. Co., 97 Ill.
537, 37 Am. Rep. 129; Miller v.
University Magazine Co., 10 Misc.
Pag. (N. V.) 311; Granite Roofing Rep. (N. Y.) 311; Granite Roofing Co. v. Michael, 54 Md. 65; Esgen v. Smith (Iowa) 84 N. W. 954; Rickerson Roller-Mill Co. v. Farrell Foundry & Machine Co. (C. C. A.) 75 Fed. 554; Bent v. Underdown, 156 Ind. 516.

Compare New Haven Trust Co. v. Gaffney, 73 Conn. 480.

Where the rights of creditors are not involved, officers of a corporation organized for the manufacture of a patented article of purely speculative value, who in good faith, and with the assent of the Min. Co., 42 Minn. 327, 18 Am. St. other stockholders, give their time Rep. 510, 2 Smith's Cas. 835, 1 and means in developing the busiother stockholders, give their time Cum. Cas. 850; Christensen v. Eno, ness of the corporation, and plac-106 N. Y. 97, 60 Am. Rep. 429, 2 ing it on a firm basis, in considis true, whether the stock was issued for cash or property at a discount,327 or for property taken at an overvaluation,328 or gratuitously. 329 An agreement by which a corporation, with the consent of all the stockholders, and without prejudice to creditors, treats stock as full-paid in consideration of the surrender by the stockholders to it of dividends declared, or of accumulated profits and increased value of its property, is binding upon the corporation.330

(b) Under particular charter, constitutional, or statutory provisions.—In some jurisdictions the general doctrine that an agreement by which a corporation issues or agrees to issue stock as full-paid upon payment in part only, in money, or in prop-

Ch. App.) 38 S. W. 93.

It has been held that a statute prohibiting a corporation from issuing stock to subscribers for less than the par value is simply to render any agreement between the corporation and its stockholders ineffective to relieve the latter from full liability to creditors of the par value of the stock, and does not render an issue of stock for less than par illegal for other purposes. Barcus v. Gates, 32 C. C. A. 337, 89 Fed. 783, construing the Virginia statute.

327 Scovill v. Thaver, 105 U. S. 143, 2 Smith's Cas. 818, 2 Keener's Cas. 897; Kenton Furnace R. & Mfg. Co. v. McAlpin, 5 Fed. 737; Hill v. Atoka Coal & Min. Co., 124 Mo. 153; Barr v. New York, Lake Erie & W. R. Co., 125 N. Y. 263.

328 Northern Trust Co. v. Columbia Straw Paper Co., 75 Fed. 936, affirmed, Dickerman v. Northern Trust Co. (C. C. A.) 80 Fed. 450; Whitehill v. Jacobs, 25 Wis. 474; Wells v. Green Bay & Mississippi

eration of a transfer to them of a Canal Co., 90 Wis. 442; Barr v. portion of unissued stock which New York, Lake Erie & W. R. Co., has no present marketable value, are not liable to the corporation for the par value of the stock. Divine v. Universal Sewing Machine Motor Attachment Co. (Tenn. Am. St. Rep. 92; Woolfolk v. January, 131 Mo. 620.

In Higgins v. Lansingh, 154 Ill. 301, the owner of an equity of redemption in land mortgaged beyond its value assigned it for the benefit of creditors, and afterwards, with their co-operation, organized a cemetery corporation, and caused the land to be conthe corporation to the extent of veyed to it, the company assuming payment of the mortgage, and issuing all its stock to the vendor and persons whom he named. It was held that, notwithstanding the amount of the mortgage exceeded the value of the land, the issue of the stock in exchange for the equity of redemption was not without consideration, and was valid as against the corporation itself. and those of its stockholders and creditors who had notice of the transaction when their rights were acquired.

> 320 Christensen v. Eno, 106 N. Y. 97, 60 Am. Rep. 429, 2 Keener's Cas. 1240, as to which see ante,. § 390(c).

330 Kenton Furnace R. & Mfg. Co.

erty, labor, or services, or by which it issues stock as a gratuity, is binding as between the corporation and the stockholders, so that the corporation cannot repudiate the agreement and recover from the stockholders as upon unpaid subscriptions, is rendered inapplicable by express charter, constitutional, or statutory provisions.

It has been held that the doctrine does not apply to subscriptions preliminary to the organization of a corporation, where the charter or law, for the protection of the public, and on grounds of public policy, requires that the capital stock of the corporation shall be subscribed in good faith as a condition precedent to the right to organize and commence business, and that the stock shall be paid in full at its par value, and that, in such a case, any agreement or stipulation that subscribers shall not be required to pay the full amount of their subscriptions. or that the amount paid shall be returned to them directly or indirectly, is not only ultra vires, but is contrary to public policy and void, as a fraud upon the law, and it cannot be set up by the subscribers, after they have become stockholders, in an action by the corporation itself to recover the full amount of the subscriptions.331 It was held, therefore, in a late Tennessee case, that a stipulation in the contracts with the subscribers to the initiatory or organization stock of a manufacturing corporation, which was required by the statutes of the state to be paid in full at its par value, by which the corporation agreed to issue to the subscribers, in addition to their shares of stock, interest bearing bonds to the full amount of their subscriptions, secured by a first mortgage on its plant, was ultra vires, without consideration, and void as against the public policy of the state, not only as against creditors, but also as between the corporation and the subscribers, and that the failure of the company to carry out the illegal stipulation could not be set up by

v. McAlpin, 5 Fed. 737; Kryger v. Andrews, 65 Mich. 405. See ante, \$ 390(f). 331 Morrow v. Nashville Iron & Steel Co., 87 Tenn. 262, 10 Am. St. Rep. 658, 2 Keener's Cas. 989.

subscribers as releasing them from liability on their subscriptions.332

In England, where it is provided by statute that "every share in any company shall be deemed and taken to have been issued and to be held subject to the payment of the whole amount thereof in cash, unless the same shall have been otherwise determined by a contract duly made in writing," it is held that an agreement to issues shares for cash at a discount, without such a contract, is not merely ultra vires, but illegal, because contrary to the prohibition of the statute. Where the shares are issued, however, the issue is not illegal and void, but the agreement by which they are paid for at less than par is so, and the holders may be compelled to pay for the shares in full, not only for the purpose of paying creditors, but also for the purpose of adjusting the rights of the stockholders inter se, on a winding up of the corporation.333

In some of the states, under the constitutional or statutory provision that no corporation shall issue stock except for money paid, labor done, or property actually received, and that all fictitious increase of stock shall be void, it is held that certificates of stock issued in violation of the prohibition, and which are altogether fictitious, nothing being paid on them, are absolutely null and void, even as between the parties, and that they do not make the persons to whom they are issued stockholders, or confer any rights or impose any liabilities upon them as such. 334 Thus, in Wisconsin, where it is provided in effect that no corporation shall issue stock except at its par value for money, labor, or property estimated at its true money value, and actu-

<sup>332</sup> Morrow v. Nashville Iron & Almada & Tirito Co., 38 Ch. Div. Steel Co., 87 Tenn. 262, 10 Am. St 415.

Rep. 658, 2 Keener's Cas. 989.

334 Kellerman v. Maier, 116 Cal.

Packet Co., [1891] 1 Ch. 66; In re Pfister, 83 Wis. 64.

<sup>416; &</sup>quot;Jefferson v. Hewitt, 103 Cal.
333 In re Railway Time Tables 624; Beitman v. Steiner Bros., 98
Pub. Co., 1895] 1 Ch. 225, 2 Smith's Ala. 241; Arkansas River L., T. & Cas. 860, affirmed, Welton v. Saf- C. Co. v. Farmers' L. & T. Co., 13 ferv, [1897] App. Cas. 299. See, Colo. 587; Clarke v. Lincoln Lumalso, In re Weymouth & C. I. Steam ber Co., 59 Wis. 655; Hinckley v.

ally received, and that all fictitious increase of stock shall be void, it was held that a certificate of stock issued gratuitously was absolutely void, and did not make the holder a stockholder, so as to give him a standing to sue as such on behalf of the corporation to compel a creditor to return bonds illegally issued to him. 335 There was a like decision in Colorado under a similar provision, where a certificate of stock was issued without any consideration.336

Where certificates of stock are not altogether fictitious, but merely in excess of the amount paid in, as where they represent shares fully paid for, and also additional shares, for which no consideration has been paid, so that they are fictitious as to the latter only, they are void, not altogether, but only as to the shares not paid for.337

When property is conveyed to a corporation in payment for stock, and certificates issued to the subscribers or purchasers, the fact that the property is overvalued does not render the transaction void, even when there is a constitutional or statutory provision that no corporation shall issue stock except at its par value, for money, labor, or property estimated at its true value, and actually received, and that all fictitious increase of stock shall be void. As between the corporation and its stockholders, it cannot be claimed that the property conveyed to them by it in payment for their stock was not a sufficient consideration 338

So long as an ultra vires or illegal contract by a corporation to issue stock at a discount, or for property or services to be taken at an overvaluation, is wholly executory, it is void, and it cannot be enforced either by or against the corporation, either at law or in equity. The parties to such a contract are in pari

<sup>335</sup> Hinckley v. Pfister, 83 Wis. 64.

<sup>336</sup> Arkansas River L., T. & C. Co. v. Farmers' L. & T. Co., 13 Colo.

Ala. 241.

<sup>338</sup> Whitehill v. Jacobs, 75 Wis. 474; Wells v. Green Bay & Mississippi Canal Co., 90 Wis. 442; Ni-crosi v. Irvine, 102 Ala. 648, 48 Am. St. Rep. 92. And see Arapahoe Cattle & Land Co. v. Stevens, 337 Beitman v. Steiner Bros., 98 13 Colo. 534; Woolfolk v. January. 131 Mo. 620.

delicto.339 A corporation cannot be compelled by mandamus to issue stock at less than its par value, in pursuance of a vote of the stockholders, but in violation of law.340

A corporation cannot maintain an action on a note given in payment of a subscription for stock, where the only consideration for the note is an agreement to issue stock at the rate of two dollars of stock for every dollar to be paid, in violation of a statutory or constitutional provision, and the stock has not yet been issued. As the agreement is void, the note is without consideration, as well as illegal.341

A subscriber for stock under an agreement which is illegal and void because it is in violation of a statutory or constitutional provision acquires no rights, by virtue of his subscription, which he can assign, so as to entitle him to maintain an action

839 Edgerton v. Electric Improvement & Construction Co., 50 N. J. Eq. 354; Garrett v. Kansas City Coal Min. Co., 113 Mo. 330, 35 Am. St. Rep. 713; Clarke v. Lincoln Lumber Co., 59 Wis. 655; Zelaya Min. Co. v. Meyer, 8 N. Y. Supp. 487; Williams v. Evans, 87 Ala. 725.

And see West Cornwall Ry. Co. v. Mowatt, 12 Jur. 407; Rogers v. Gross, 67 Minn. 224.

Compare Otter v. Brevoort Petroleum Co., 50 Barb. (N. Y.) 247.

A party to a contract by which a large amount of paid-up capital stock in a corporation, to be organized for the development of certain lands, is to be issued to him in exchange for his equitable rights in options on such lands, and for his services in promoting the corporation, cannot sue in equity to enforce the contract, where it appears that his interest in the lands and his services, when taken together, are not a fair equivalent press provisions of the constitu- son v. Hewitt, 103 Cal. 624.

tion and statutes of the state, as well as the general policy of the law, requiring that the subscribers to corporate stock shall pay in money or money's worth. Garrett v. Kansas City Coal Min. Co., 113 Mo. 330, 35 Am. St. Rep. 713.

340 State v. Timken, 48 N. J. Law.

341 Alabama Nat. Bank v. Halsey, 109 Ala. 196. Compare Pacific Trust Co. v. Dorsey, 72 Cal. 55; First Nat. Bank of Baldwinsville v. Cornell, 8 App. Div. (N. Y.) 427. As to these two cases, see ante, §

In California, under a statutory prohibition against the issue of stock except for money paid, labor done, or property actually received, it was held that a certificate of stock of a railroad company issued upon payment by a note conditioned upon the completion of the road within a given time was illegal and void, and that the note therefor the face value of the stock for was without consideration, and which he is to receive, and where void, and the assignees thereof the issue of the stock under such (the note being nonnegotiable) circumstances contravenes the ex- could not recover upon it. Jefferagainst the assignee upon an executory contract to pay for the rights assigned.342

(c) Fraudulent and unauthorized issue by directors.-If the directors or managing officers of a corporation issue its stock fraudulently or without authority for less than its par value in money or property, the corporation may undoubtedly hold them liable in damages, and if it has been issued to themselves, it may compel them to surrender or return the same or account for its value, unless it is barred by laches or ratification. Even when the stock is issued to third persons, it may sue to cancel the same or recover the full value, unless they are bona fide holders.343

# Effect as against the subscribers or purchasers.

In the absence of some special statutory or constitutional provision, an agreement between a corporation and the subscribers for or purchasers of its stock, under which the stock is issued at less than par, or for property taken at an overvaluation, with the understanding that it shall be regarded as full-paid, is binding as between the parties thereto, not only as against the corporation,344 but also as against the subscribers or purchasers,345 although invalid as against dissenting stockholders 346 and subsequent bona fide creditors.347

In some jurisdictions, however, as we have seen, under the constitutional or statutory provision that no corporation shall issue stock except for money paid, labor done, or property actually received, and that all fictitious increase of stock shall be void, or other provisions on the subject, it is held that certificates issued in violation of the prohibition, and which are fictitious, are absolutely void, and do not make the persons to whom they are issued stockholders, or confer upon them any rights

<sup>342</sup> Williams v. Evans, 87 Ala. 725.

<sup>848</sup> See post, chapter xxiv.

<sup>344</sup> Ante, § 395.
345 Scovill v. Thayer, 105 U. S.
143, 2 Smith's Cas. 818, 2 Keener's

Cas. 897; Bruner v. Brown, 139 Ind. 600; Callanan v. Windsor, 78 Iowa, 193; Walburn v. Chenault, 43 Kan. 352.

<sup>346</sup> Post, § 397. 347 Post, § 401.

whatever, and any promise made by them in consideration of the issue of such a certificate is without consideration and void.348

So long as an ultra vires or illegal contract for the issue of watered stock is executory, the corporation cannot enforce it against the subscribers or purchasers, either by a suit in equity or by an action at law, for no action will lie to enforce an executory ultra vires or illegal contract.349

In England there is a conflict in the decisions as to whether a person to whom stock has been illegally issued at a discount may repudiate his subscription and recover what he has paid.350 In Wisconsin it has been held that, since the transaction is illegal, and the parties in pari delicto, such an action will not lie. but the courts will leave the parties where they have placed themselves. According to this doctrine, although the certificate of stock issued to a subscriber or purchaser in violation of a statutory or constitutional prohibition is void, and confers no rights upon him as against the corporation, he cannot maintain an action against it to recover what he has paid therefor.351

348 Ante, § 391; Jefferson v. Hewitt, 103 Cal. 624; Kellerman v. ber Co., 59 Wis. 655; Zelaya Min. Maier, 116 Cal. 416; Beitman v. Co. v. Meyer, 8 N. Y. Supp. 487; Steiner Bros., 98 Ala. 241; Arkansas River L., T. & C. Co. v. Farmers' L. & T. Co., 13 Colo. 587; bles Pub. Co., 42 Ch. Div. 98; In Clarke v. Lincoln Lumber Co., 59 Ch. Mind. 224. Wis. 655; Hinckley v. Pfister, 83

An agreement with subscribers that, for every share paid for, two or more shares shall be issued, is void under the Minnesota statute as between the subscribers, and no equitable rights in their favor can arise out of it. Rogers v. Gross, 67 Minn. 224.

349 West Cornwall Ry. Co. v. Mowatt, 12 Jur. 407; Edgerton v. Electric Improvement & Construc-Knox v. Childersburg Land Co., 86 is afterwards declared void by the

bles Pub. Co., 42 Ch. Div. 98; In re Almada & Tirito Co., 38 Ch. Div. 415; In re Zoedone Co., 60 L. T. 383; In re Midland Electric Light & Power Co., 60 L. T. 666.

351 Clarke v. Lincoln Lumber Co., 59 Wis. 655.

But when stock in a corporation (ante, § 391), and not enforceable is sold in good faith for less than its full value, and a certificate issued therefor, which is void because issued for stock not fully paid, the consideration paid may be recovered. Potter v. Necedah Lumber Co., 105 Wis. 25.

It has been held that, while a pertion Co., 50 N. J. Eq. 354; Garrett son who purchases stock in a forv. Kansas City Coal Min. Co., 113 eign corporation, issued at less Mo. 330, 35 Am. St. Rep. 713; than par, in violation of the stat-State v. Timken, 48 N. J. Law, 87; utes of the foreign state, and which

Whether or not one who has entered into a contract with a corporation to take stock at a discount in violation of its charter or of statutory or constitutional provisions can repudiate the contract, and recover what he has paid thereunder, before the stock has been issued, depends upon whether the courts in the particular jurisdiction recognize the doctrine that where an illegal agreement is not malum in se, but merely malum prohibitum, a locus poenitentiae remains, and so long as the illegal object has not been carried out by performance of the agreement, it may be repudiated, and money paid under it recovered back.352 This doctrine was recognized in a federal case which went up to the supreme court of the United States, and it was held that a person who had subscribed for stock in furtherance of an illegal increase of stock could repudiate the agreement before issue of the stock, and recover money paid Several of the state courts, however, have refused under it.353 to recognize such a doctrine, and have held that the courts will leave the parties, being in pari delicto, in the position in which they have placed themselves.354

There may be fraud and illegality in an issue of stock aside from the mere fact that it is not paid for, so as to prevent any rights arising in favor of the stockholders. Where a stockvards company was organized by the officers of a railroad com-

lations to the corporation, and a Ct. R. 458. delay of eight years before demanding the return of the money paid bars his right to rescind and recover the same. Hallett v. New England Roller-Grate Co., 105 Fed.

It would seem, contrary to the dictum in the case just cited, that the stockholder cannot recover at pire Spring Co., 57 N. Y. 518; Goff all in such a case, aside from any v. Hawkeye Pump & Windmill Co., all in such a case, aside from any

courts of such state, may have the question of laches, for a subscribright to rescind for mistake, and er for stock in a foreign corporarecover what he paid for the stock, tion should be deemed, in so far on the ground that his ignorance of the laws of the other state was poration is concerned, a resident ignorance of fact, he must have of the domicile of the corporation. used reasonable diligence to assert the domicile of the corporation. See McKean v. New York National certain the law governing his re-Building & Loan Ass'n, 24 Pa. Co.

352 See Clark, Contracts, 494.

353 Knowlton v. Congress & Empire Spring Co., 14 Blatchf. 364, Fed. Cas. No. 7,903, affirmed sub. nom. Spring Co. v. Knowlton, 103 U. S. 49.

354 Knowlton v. Congress & Em-

pany and others, and the only means put into the same was by the railroad company, through its officers, who controlled the stock-yards company, and the stock-yards company issued its full capital stock, and a part thereof was used as a corruption fund for the purpose of corrupting certain public officials in the interest of the company, and the balance was divided between certain members of the company without any payment therefor, it was held that the issue of the stock was in violation of law, and in fraud of the rights of the stockholders of the railroad company, and vested in the recipients of the same no rights which a court of equity would enforce or protect.355

# § 397. Effect as against dissenting stockholders.

In the absence of an express provision or agreement to the contrary, persons who have become stockholders in a corporation by subscribing for or purchasing shares, and paying or agreeing to pay for them, have a right to assume that other stockholders have come in on the same terms, and contributed or agreed to contribute a like amount of capital in proportion to their shares, and they also have a right to expect that subsequent subscribers or purchasers will come in on the same terms. Any secret agreement, therefore, between the officers of the corporation and subscribers or purchasers of shares, although authorized or ratified by a majority of the stockholders, by which such subscribers or purchasers have been permitted to acquire their shares without payment, or on part payment only, or by which they are given the right to withdraw and receive back what they have paid, is a fraud upon subsequent bona fide subscribers or purchasers, and void as to them. And if

surrendered, a portion of the new at law or in equity.

62 Iowa, 691. And see Clarke v. certificates to be used for the pur-Lincoln Lumber Co., 59 Wis. 655. pose of corrupting certain public 355 Tobey v. Robinson, 99 III, 222. officers in the interest of the com-In this case the holder of certifi- pany, and the rest to be returned cates issued by the stock-yards com- to the holder. It was held that, pany surrendered the same to an as the agreement was illegal and officer of the company under an void, the return of the balance of agreement that new certificates the certificates or payment of damshould be issued in lieu of those ages could not be enforced either the corporation refuses to enforce full payment, or repays what has been paid in, they may maintain a suit in equity on behalf of themselves and other stockholders to compel payment in full or repayment of what has been withdrawn.356

If a corporation is about to issue stock without receiving payment in full, in violation of the common-law rights of stockholders, or in violation of a charter, statutory, or constitutional provision, a dissenting stockholder may maintain a suit in equity on behalf of himself and other stockholders to enjoin it from doing so.357 Or, if the stock has already been issued, he may maintain a suit to annul and cancel the same, 358 provided he is not barred by laches or acquiescence, 359 or the rights of bona fide purchasers for value.360

The issue of watered stock by a corporation is no ground for proceedings by a dissenting stockholder to have the corporation wound up and dissolved, unless it is made so by statute.361

### § 398. Effect as to stockholders participating, consenting, or acquiescing.

When a corporation has issued its stock as full-paid, without receiving its par value in money or property, the transaction cannot be assailed by stockholders who participated, consented, or acquiesced. They are estopped.<sup>362</sup> And a stockholder who

356 Melvin v. Lamar Ins. Co., 80 man, Clinton & S. R. Co. v. Kelly, Ill. 446, 22 Am. Rep. 199, 2 Keen- 77 Ill. 426; Kimball v. New Enger's Cas. 1197, 2 Smith's Cas. 852; White Mountains R. Co. v. Eastman, 34 N. H. 124; Blodgett v. Morrill, 20 Vt. 509. And see post, § 467(c).

357 Fitzpatrick v. Dispatch Publishing Co., 83 Ala. 604. And see Langan v. Francklyn, 20 N. Y. Supp. 404; Donald v. American Smelting & Refining Co. (N. J.) 48 Atl. 771, 1116.

858 Fisk v. Chicago, Rock Island
 P. R. Co., 53 Barb. (N. Y.) 513;

land Roller Grate Co., 69 N. H. 485.

359 Foster v. Belcher's Sugar-Refining Co., 118 Mo. 238; Keeney v. Converse, 99 Mich. 316. And see Taylor v. South & North Alabama R. Co., 13 Fed. 152.

360 See post, chapter xxiii.

361 In re Pioneers of Mashonaland Syndicate, 68 L. T. 163; In re Gold Co., 11 Ch. Div. 701; Morrison v. Globe Panorama Co., 28 Fed. 817.

362 Wood v. Corry Water-Works Parsons v. Joseph, 92 Ala. 403; Co., 44 Fed. 146; Washburn v. Na-Perry v. Tuskaloosa Cotton Seed tional Wall Paper Co. (C. C. A.) Oil Mill Co., 93 Ala. 364; Campbell 81 Fed. 17; Nicrosi v. Calera Land v. Morgan, 4 Bradf. (Ill.) 100; Gil- Co., 115 Ala. 429; Winston v. Dor-

does not object within a reasonable time, when he has knowledge of the transaction, will be deemed to have acquiesced.363

This principle not only applies when the participating, consenting, or acquiescing stockholder attacks the transaction as a stockholder, as where he seeks, by reason of his relation as stockholder, to set the transaction aside and cancel the stock,364 or to compel payment of its full par value, or the difference between its par value and what has been paid,365 or claims that the holder of such stock had no right to vote thereon at a meeting of the stockholders of the corporation, 366 but it also applies where he seeks relief as a creditor of the corporation, and as such claims the right to compel the holders of such stock to pay the difference between the amount paid by them and the par value of the stock.367

If a person subscribes for stock with the understanding that he is to be released from liability on his subscription, and all the stockholders assent to the agreement, payment of the subscription will be required, notwithstanding the agreement, if it is necessary in order to satisfy the claims of creditors of the corporation;368 but if its enforcement is not necessary for the

sett Pipe & Paving Co., 129 Ill. 64, 363 Taylor v. South & North Ala-2 Smith's Cas. 857, 2 Keener's Cas. bama R. Co., 13 Fed. 152; Keeney 2 Smith's Cas. 651, 2 Reener's Cas. 1212; Green v. Abietine Medical Co., 96 Cal. 322; Lorillard v. Clyde, 86 N. Y. 384; Mathis v. Pridham, 1 Tex. Civ. App. 58; Callanan v. Windsor, 78 Iowa, 193; Clark v. American Coal Co., 86 Iowa, 436; Schilling & Schneider Brewing Co. v. Schneider, 110 Mo. 83; Woolfolk v. January, 131 Mo. 620; Ten Eyck v. Pontiac, Oxford & P. A. R. Co., 114 Mich. 494; Wisner v. Delhi Land & Improvement Co., 46 La. Ann. 1223; Ambler v. Archer, 1 App. D. C. 94; Knoop v. Bohmrich, 49 N. J. Eq. 82; Bent v. Underdown, 156 Ind. 516; Esgen v. Smith (Iowa) 84 N. W. 954; Drake v. Mich. 494; Woolfolk v. January, New York Suburban Water Co., 26 131 Mo. 620; Ambler v. Archer, 1 App. Div. (N. Y.) 499; Richard-App. D. C. 94; Knoop v. Bohmson v. Chicago Packing & Provirich, 49 N. J. Eq. 82. sion Co. (Cal.) 63 Pac. 74.

v. Converse, 99 Mich. 316.

364 Clark v. American Coal Co.,

86 Iowa, 436.

365 Green v. Abietine Medical Co., 96 Cal. 322; Winston v. Dorsett Pipe & Paving Co., 129 III. 64, 2 Smith's Cas. 857, 2 Keener's Cas. 1212; Esgen v. Smith (Iowa) 84 N. W. 954.

366 Wisner v. Delhi Land & Improvement Co., 46 La. Ann. 1223.

367 Nicrosi v. Calera Land Co., 115 Ala. 429; Callanan v. Windsor, 78 Iowa, 193; Mathis v. Pridham, 1 Tex. Civ. App. 58; Ten Eyck v. Pontiac, Oxford & P. A. R. Co., 114 368 Post, § 401.

payment of creditors, the agreement is binding as against the corporation and the other stockholders. 369 And it follows that, in winding up a corporation, and providing for the payment of creditors, all the other stockholders will be required to pay in what may remain due on their subscriptions before payment will be required of one who subscribes with the understanding, consented to by all the stockholders, that he should be released from liability on his subscription.370

The principle that participating or consenting stockholders are estopped to complain of an issue of watered or fictitiously paid up stock applies even when the stock is issued in violation of an express charter, statutory, or constitutional provision.<sup>371</sup>

In England, where it is provided by statute that "every share in any company shall be deemed and taken to have been issued and to be held subject to the payment of the whole amount thereof in cash, unless the same shall have been otherwise determined by a contract duly made in writing," it has been held that an issue of shares at a discount, without such a contract in writing, is not only ultra vires, but illegal, because contrary to the prohibition of the statute that the agreement not to require payment in full is void, and that persons who take shares at a discount are not only liable to be called upon to contribute, if necessary, for the benefit of creditors, to the extent of the difference between the amount paid and the par value of the shares, but are also liable for the purpose of adjusting the rights of the stockholders inter se.372

### Effect as against transferees. § 399.

A transferee of stock in a corporation occupies the same position as his transferrer with respect to the right to complain

369 Winston v. Dorsett Pipe & Paving Co., 129 Ill. 64, 2 Smith's Cas. 857, 2 Keener's Cas. 1212.

Cas. 857, 2 Keener's Cas. 1212.

371 Wood v. Corry Water-Works Co., 44 Fed. 146, and other cases cited in note 362, supra.

372 In re Railway Time Tables 370 Winston v. Dorsett Pipe & Pub. Co., [1895] 1 Ch. 255, 2 Smith's Paving Co., 129 Ill. 64, 2 Smith's Cas. 860, affirmed, Welton v. Saffery, [1897] App. Cas. 299.

of an issue of watered or fictitiously paid up stock, and is therefore estopped to complain if his transferrer was estopped. This is true, whether he is a transferee of shares of the watered stock, or a transferee of shares of other stock, which was held by a participating or consenting stockholder; and it is true notwithstanding the fact that he purchased the stock in good faith and in ignorance of the fraudulent or unlawful issue.373

As we shall hereafter see, however, a purchaser of watered or fictitiously paid up stock, without notice, may maintain an action to recover damages sustained by him, either against the transferrer, if the latter knew the character of the stock, or against the promoters, or the directors or other officers who issued the same, or against the corporation itself if it can be regarded as a party to the fraud.374 And if the seller of watered stock was a party to the fraudulent or illegal issue, or if he had knowledge of the fraud or illegality, the purchaser may rescind and set up the fraud to defeat an action for the price; or if the price, or any part thereof, has been paid, he may rescind and recover the same.375

If a subscription for stock is illegal and void because of an agreement to issue the stock in violation of a constitutional or statutory provision, no relief can be granted upon an executory contract to pay for a transfer of the subscriber's rights under the subscription. 376

The liability of transferees of watered or fictitiously paid up

v. Lansingh, 154 Ill. 301; Callanan v. Windsor, 78 Iowa, 193; Clark v. American Coal Co., 86 Iowa, 436; Barr v. New York, Lake Erie & W. R. Co., 125 N. Y. 263; In re Syracuse, Chenango & N. Y. R. Co., 91 N. Y. 1; Drake v. New York 725.

373 Wood v. Corry Water-Works Suburban Water Co., 26 App. Div. street R. Co., 78 Fed. 526; Higgins Pious Suburban Water Co., 26 App. Div. Co., 44 Fed. 146; Flagler Engraving Machine Co. v. Flagler, 19 Fed. Abb. N. C. (N. Y.) 419; Nott v. 468; Venner v. Atchison, Topeka & Clews, 14 Abb. N. C. (N. Y.) 437; S. F. R. Co., 28 Fed. 581; Brown Miller v. University Magazine Co., v. Duluth, Missabe & N. Ey. Co., 10 Misc. Rep. (N. Y.) 311; Wal53 Fed. 889; Church v. Citizens' burn v. Chenault, 43 Kan. 352; Street R. Co., 78 Fed. 526; Higgins Ffooks v. South Western Ry. Co., 1 Smale & G. 142.

Contra, Parsons v. Joseph, 92 Ala. 403. And see post, § 570.

374 Post, § 570. 375 Post. § 570.

376 Williams v. Evans, 87 Ala.

stock to creditors of the corporation is considered in a subsequent section.377

#### § 400. Issue to directors or other officers.

The rule that the directors and managing officers of a corporation are to be held to strict good faith in all dealings between themselves and the corporation applies as well when they issue stock to themselves as in other cases. If they act in bad faith, and obtain a profit or advantage not enjoyed by other stockholders, they may be called to account, or the transaction may be set aside.378

They may purchase stock, however, if they act in good faith, and they will incur no liability to the corporation or the other stockholders, in the absence of a statute, even when they purchase stock at less than par, where it appears that they acted in good faith and in the interest of the company, particularly where they have obtained no profit or advantage for themselves from the transaction. In a late Ohio case, in which stockholders of a corporation who had paid par for their stock sought to hold the directors and managing officers and others liable upon stock taken by them at less than par for the difference between what they paid and the par value, it appeared that the corporation at the time, and before the stock was taken, was deeply in debt, and pressed for money to continue its business; that a large part of its capital stock remained unsubscribed, a great part of which was created by an unauthorized increase of the same, for which the directors and managing officers were chiefly responsible, though acting in good faith, and in the belief that their action was regular; that the directors and managing officers, believing that the only practical means of obtaining money to relieve the necessities of the cor-

Pa. St. 563: Arkansas Valley Agricultural Soc. v. Eichholtz, 45 Kan. gomery Co., 31 Pa. St. 78, 72 Am. 380. And see ante, § 388; post, Dec. 726; Morris v. Stevens, 178 chapter xxiv.

<sup>377</sup> Post, § 401(k).

poration was by disposing of this stock, and after having made diligent but unsuccessful efforts to dispose of it at par, offered it at a large discount to all of its stockholders, and generally to others, without takers, and then they themselves, and some others, without intending to secure any personal advantage, but with a view to aid the corporation, took parts of the stock at the discount price, either paying cash therefor, or cancelling debts due to them from the corporation, but did not then or afterwards derive any profit on account of the stock. Under these circumstances it was held that bad faith was not imputable to them with respect either to such increase of the stock or their acquisition of it; that, on the corporation becoming insolvent, the difference between the discount price and the par value of the stock thus purchased should not be regarded as assets of the corporation, as between those who bought at a discount and those who did not; and that the holders of previously issued stock, for which they had paid par, should not be allowed to assert the invalidity of the issue of the discounted stock without consenting that its purchasers be placed in statu  $quo.^{379}$ 

#### § 401. Effect as against creditors.

(a) In general.—It was formerly held in England that, where stock was issued by a corporation as full-paid upon payment of less than par value, and the corporation afterwards became insolvent, and was wound up, the court could not compel the holders of the stock to pay up, for the benefit of creditors of the corporation, the difference between the par value of the stock and the amount actually paid in. 380 These decisions proceeded upon the ground that, if the transaction was invalid,

<sup>379</sup> Peter v. Union Mfg. Co., 56 Tin & Copper Min. Co., 14 Ch. Div. Ohio St. 181, 2 Keener's Cas. 1216. 390; In re Dronfield Silkstone Coal Co., 17 Ch. Div. 76; In re Ince Hall 380 In re British Provident Life Rolling Mills Co., 23 Ch. Div. 545, 6 Guarantee Ass'n, 5 Ch. Div. 306; note; In re Great Northern & Mid-In re Wedgwood Coal & Iron Co., land Coal Co., 3 De Gex, J. & S. 367, 7 Ch. Div. 94; In re Ambrose Lake 2 Smith's Cas. 817.

because ultra vires or in fraud of subsequent creditors, it was invalid in toto; that the court could set it aside altogether, requiring the stock to be returned to the corporation, and what was paid therefor, if anything, returned to the stockholders; but that it could not alter the agreement between the corporation and the stockholders, and substitute or create an agreement to pay the full par value of the shares. In other words, it was held that "the transaction might be undone but could not be modelled."381 In the later cases, however, the courts have repudiated this doctrine, and it has been held by the house of lords, as well as by the lower courts, that where a corporation illegally issues its stock for less than par, the stockholders, upon the insolvency and winding up of the company, may be compelled to pay the full par value, if necessary for the payment of creditors.382

In this country it is well settled that a court of equity, and in some jurisdictions, under the statutes, a court of law, may compel full payment for stock, contrary to the actual agreement between the stockholders and the corporation, when such payment is necessary to prevent a fraud upon the creditors of the corporation. Since the capital stock of a corporation constitutes the basis of its credit, persons dealing with a corporation have a right to assume, unless there is something to show the contrary, that the full amount of its issued capital stock has been actually paid in or secured to be paid in, either in money or its equivalent, so that it may be reached, if necessary. for the satisfaction of corporate debts. As a general rule, therefore, any agreement between a corporation and its stockholders, under which its capital stock is issued and falsely held

<sup>382</sup> Ooregum Gold Min. Co. v. v. Saffery, [1897] App. Cas. 299; In Roper, [1892] App. Cas. 125, 66 L. re New Eberhardt Co., 43 Ch. Div. T. 427, 2 Cum. Cas. 247; In re 118; In re Almada Tirito Co., 38 Addlestone Linoleum Co., 37 Ch. Ch. Div. 415.

out to the public as full-paid, when it is not paid for at all, or is paid for in part only, either in money or in property, labor, or services, while it may be binding as between the corporation and the persons to whom the stock is issued, or their transferees,383 and as against other stockholders who participate, consent, or acquiesce,384 and as against creditors who have not dealt with the corporation on the faith of such stock being full-paid,385 is invalid as against creditors who have dealt with the corporation on the faith of the stock being full-paid; and the agreement will be set aside or disregarded in equity, or, by statute in some jurisdictions, even at law, and full payment for the stock enforced, at the instance of creditors, or of a receiver or other person representing them, if such payment is necessary for the satisfaction of their claims. This doctrine has been applied, not only when there have been express charter, statutory, or constitutional provisions requiring stock to be full-paid, but also, on the ground of fraud, in the absence of express provisions to this effect.386

383 Ante, §§ 395, 396, 399.

384 Ante. § 398.

385 See infra, this section, (j). 386 United States: Sawyer v. Hoag, 17 Wall. (U.S.) 610, 2 Smith's Cas. 812, 1 Cum. Cas. 818; Ogilvie v. Knox Ins. Co., 22 How. (U.S.) 380, 1 Cum. Cas. 814; Upton v. Tribilcock, 91 U.S. 45, 1 Cum. Cas. 824; Webster v. Upton, 91 U. S. 65; Hawley v. Upton, 102 U. S. 314; Scovill v. Thayer, 105 U. S. 143, 2 Keener's Cas. 897, 2 Smith's Cas. 818; Richardson v. Green, 133 Milling Co., 79 Fed. 459; Ricker- 162 III. 402. son Roller-Mill Co. v. Farrell Foun-

dry & Machine Co. (C. C. A.) 75 Fed. 554.

Alabama: Elyton Land Co. v. Birmingham Warehouse & Elevator Co., 92 Ala. 407, 25 Am. St. Rep. 65, 1 Cum. Cas. 870; Roman v. Dimmick, 115 Ala. 233.

California: Walter v. Merced Academy Ass'n, 126 Cal. 582.

Connecticut: New Haven Trust Co. v. Gaffney, 73 Conn. 480.

Illinois: Union Mut. Life Ins. Co. v. Frear Stone Mfg. Co., 97 Ill. 537, 37 Am. Rep. 129; Coleman v. U. S. 30; Fogg v. Blair, 139 U. S. Howe, 154 Ill. 458, 45 Am. St. Rep. 118; Handley v. Stutz, 139 U. S. 133; Great Western Tel. Co. v. 417, 2 Keener's Cas. 976, 2 Smith's Gray, 122 Ill. 630; Bates v. Great Cas. 844, 1 Cum. Cas. 855; Cam. Western Tel. Co., 134 Ill. 536; Alden v. Stuart, 144 U. S. 104; Lloyd ling v. Wenzel, 133 Ill. 264; Hickv. Preston, 146 U. S. 630; Marsh ling v. Wilson, 104 III. 54; Sprague v. Burroughs, 1 Woods, 463, Fed. v. National Bank of America, 172 Cas. No. 9,112; In re Glen Iron Ill. 149, 64 Am. St. Rep. 17; Na-Works, 17 Fed. 324; Grant v. East tional Bank of America v. Pacific & West R. Co., 13 U. S. App. 1, 54 Ry. Co., 66 Ill. App. 320; World's Fed. 569; Addison v. Pacific Coast Fair E. & T. Boat Co. v. Gasch,

Indiana: See Clow v. Brown, 150

"Any arrangement," said the court of appeals of Maryland, "among the stockholders, or those in charge of the affairs of the corporation, by which the stock is but nominally paid for, whether in money or property, the corporation not in fact get-

Ind. 185; Bent v. Underdown, 156 Ind. 516. But as to payment in property, see infra, this section, (d).

Iowa: Osgood v. King, 42 Iowa, 478; Jackson v. Traer, 64 Iowa, 469, 52 Am. Rep. 449; Wishard v. Hansen, 99 Iowa, 307, 61 Am. St. Rep. 238; Chisholm Bros. v. Forney, 65 Iowa, 333; Boulton Carbon Co. v. Mills, 78 Iowa, 460; Stout v. Hubbell, 104 Iowa, 499; Tuthill Spring Co. v. Smith, 90 Iowa, 331.

Kentucky: Haldeman v. Ainslie,

82 Ky. 395.

Louisiana: Belknap v. Adams,

49 La. Ann. 1350.

Maine: Libby v. Tobey, 82 Me. 397; Barron v. Burrill, 86 Me. 66. Maryland: Crawford v. Rohrer, 59 Md. 599; Brant v. Ehlen, 59 Md. 1.

Michigan: Peninsular Sav. Bank of Detroit v. Black Flag Stove Polish Co., 105 Mich. 535.

Minnesota: Wallace v. Carpenter Electric Heating Mfg. Co., 70 Minn. 321, 68 Am. St. Rep. 530; Hastings Malting Co. v. Iron Range Brewing Co., 65 Minn. 28, 2 Smith's Cas. 831; Hospes v. Northwestern Mfg. & Car Co., 48 Minn. 174, 31 Am. St. Rep. 637, 2 Keener's Cas. 1890, 1 Cum. Cas. 885; First Nat. Bank of Deadwood v. Gustin Minerva Consolidated Min. Co., 42 Minn. 327, 18 Am. St. Rep. 510, 2 Smith's Cas. 835, 1 Cum. Cas. 850.

Missouri: Guerney v. Moore, 131 Mo. 650; Van Cleve v. Berkey, 143 Mo. 109; Hill v. Atoka Coal & Min.

Co., 124 Mo. 153.

Montana: Kelly v. Fourth of July Min. Co., 21 Mont. 291.

Nebraska: Gilkie & Anson Co. v. Dawson Town & Gas Co., 46 Neb. 333

New Jersey: Wetherbee v. Baker, 35 N. J. Eq. 501; Hebberd v. Southwestern Land & Cattle Co., 55 N. J. Eq. 18; Lee v. Heppenheimer, 55 N. J. Eq. 240.

New York: See Sagory v. Dubois, 3 Sandf. Ch. 466; Herbert v. Uhl, 20 N. Y. Supp. 743; Montgomery v. Brush Electric Illuminating Co., 48 App. Div. (N. Y.) 12, affirmed 168 N. Y., mem.; White, Corbin & Co. v. Jones, 167 N. Y. 158.

North Carolina: Clayton v. Ore Knob Co., 109 N. C. 385.

Ohio: Gates v. Tippecanoe Stone Co., 57 Ohio St. 60.

Pennsylvania: Freeman v. Stine, 15 Phila. 37.

Tennessee: Kelley Bros. v. Fletcher, 94 Tenn. 1.

Texas: Nenny v. Waddill, 6 Tex. Civ. App. 244; Mathis v. Pridham, 1 Tex. Civ. App. 58.

Utah: Henderson v. Turngren, 9 Utah, 432; Salt Lake Hardware Co. v. Tintic Milling Co., 13 Utah, 423. Virginia: Martin v. South Salem Land Co., 94 Va. 28.

Washington: Manhattan Trust Co. of New York v. Seattle Coal & Iron Co., 16 Wash. 499; Adamant Mfg. Co. of America v. Wallace, 16 Wash. 614; Barto v. Nix, 15 Wash. 563; Dunlap v. Rauch (Wash.) 64 Pac. 807.

Wisconsin: Gogebic Inv. Co. v. Iron Chief Min. Co., 78 Wis. 427, 23 Am. St. Rep. 417; National Bank of Merrill v. Illinois & Wisconsin Lumber Co., 101 Wis. 247; Shaw v. Gilbert (Wis.) 86 N. W. 188.

It has been held that the stockholders are also liable for interest from the time when the subscriptions should have been paid. Shaw v. Gilbert (Wis.) 86 N. W. 188.

It is no defense as against the claim of creditors for full payment that the stock was not in fact worth more than was paid for it. Adamant Mfg. Co. v. Wallace, 16 Wash. 614; Martin v. South Salem Land Co., 94 Va. 28; and other cases above cited.

ting the benefit of the price in good faith, will be regarded as a sham and not as a valid payment, as against the creditors of the corporation, however it may be regarded as between the corporation and the subscriber."387

In a late case in the supreme court of the United States it "It is the settled doctrine of this court that the was said: trust arising in favor of creditors by subscriptions to the stock of a corporation cannot be defeated by a simulated payment of such subscription, nor by any device short of an actual payment in good faith. And while any settlement or satisfaction of such subscription may be good as between the corporation and the stockholders, its is unavailing as against the claims of the creditors."388

And in a late Minnesota case it was said: "A certificate for paid-up shares in a corporation is simply a written statement in the name of the corporation that the holder thereof is a stockholder, and that the full par value of his shares has been paid to the corporation. If the shares in fact have not been so paid for, the certificate that they have been is a false representation that the assets of the corporation have been increased to the amount of the par value of the stock so issued. And when a corporation represents that it has a paid-up capital of a given amount, it represents to the business world that at the time it issued the stock it received money or property to the full par value of its stock. The issuing of the stock of a corporation as paid-up when it is not so in fact is a public

599.

387 Crawford v. Rohrer, 59 Md. see § 401(g)], was intended to overrule or qualify in any way the wholesome principle adopted by 388 Mr. Justice Brown, in Cam- this court in the earlier cases, espeden v. Stuart, 144 U. S. 104, 113. cially as applied to the original It was further said in this case: subscribers to stock. The later "Nothing that was said in the re- cases were only intended to draw cent cases of Clark v. Bever, 139 a line beyond which the court was U. S. 96 (2 Keener's Cas. 967); unwilling to go in fixing a liability Fogg v. Blair, 139 U. S. 118; or upon those who had purchased Handley v. Stutz, 139 U. S. 417 (2 stock of the corporation, or had Keener's Cas. 976, 2 Smith's Cas. taken it in good faith in satisfac-844, 1 Cum. Cas. 855), [as to which tion of their demands." and a private wrong—a cheat and a fraud—which enables the corporation to obtain credit and property by false pretenses."389

Fraud is the only true basis of this doctrine.—Some of the courts, including the supreme court of the United States, in its earlier opinions, have based this doctrine upon the ground that the subscribed capital stock of a corporation is in equity a trust fund for the payment of its debts, and that no agreement between a corporation and its stockholders can affect the wight of creditors to so treat it. 390 It is now practically settled, however, that this is not the basis of the doctrine, for neither the unpaid subscriptions of a corporation nor its other assets are in any proper sense a trust fund for creditors.391 The true and only ground of the doctrine is fraud. 392 arrangement between the stockholders of a corporation and the corporation, by which the former are to pay nothing at all, or less than par, either in money or property, for shares of stock which are issued and represented to the public as being full-paid, is clearly a fraud upon persons who deal with the corporation on the faith of such representation, and it requires the application of no new principle to enable a court of equity to prevent creditors from being defrauded by compelling the

389 Wallace v. Carpenter Electric Heating Mfg. Co., 70 Minn. 321, 329, 68 Am. St. Rep. 530, 535.

390 In Scovill v. Thayer, 105 U.S. 143, 2 Keener's Cas. 897, 2 Smith's Cas. 818, it was said: "The reastance require it to be paid."

391 See post, chapter xxv. 392 Hospes v. Northwestern Mfg. & Car Co., 48 Minn. 174, 31 Am. St. Rep. 637, 1 Cum. Cas. 885; O'Bear Jewelry Co. v. Volfer & Co., 106 Ala. 205, 54 Am. St. Rep. 31, 2 Smith's Cas. 831; Hastings Maltson is, that the stock subscribed is ing Co. v. Iron Range Brewing Co., considered in equity as a trust fund 65 Minn. 28, 2 Smith's Cas. 831; for the payment of creditors. First Nat. Bank of Deadwood v. \* \* \* It is so held out to the Gustin Minerva Consolidated Min. public, who have no means of Co., 42 Minn. 327, 18 Am. St. Rep. knowing the private contracts 510, 2 Smith's Cas. 835, 1 Cum. made between the corporation and Cas. 850; Coleman v. Howe, 154 its stockholders. The creditor has, Ill. 458, 45 Am. St. Rep. 133; Holtherefore, the right to presume lins v. Brieffeld Coal & Iron Co., that the stock subscribed has been 150 U. S. 371; Handley v. Stutz, or will be paid up, and if it is not, 139 U. S. 417, 2 Keener's Cas. 976, a court of equity will at his in- 2 Smith's Cas. 844, 1 Cum. Cas. 855.

stockholders to make their representation good. Creditors not defrauded cannot complain.<sup>393</sup>

This question was considered in a Minnesota case. Mitchell said: "It is difficult, if not impossible, to explain or reconcile these cases upon the 'trust-fund' doctrine, or, in the light of them, to predicate the liability of the stockholder upon that doctrine. But by putting it upon the ground of fraud, and applying the old and familiar rules of law on that subject to the peculiar nature of a corporation and the relation which its stockholders bear to it and to the public, we have at once rational and logical ground on which to stand. capital of a corporation is the basis of its credit. It is a substitute for the individual liability of those who own its stock. People deal with it and give it credit on the faith of it. They have a right to assume that it has paid-in capital to the amount which it represents itself as having; and if they give it credit on the faith of that representation, and if the representation is false, it is a fraud upon them; and in case the corporation becomes insolvent, the law, upon the plainest principles of common justice, says to the delinquent stockholder, 'Make that representation good by paying for your stock.' It certainly cannot require the invention of any new doctrine in order to enforce so familiar a rule of equity. It is the misrepresentation of fact in stating the amount of capital to be greater than it really is that is the true basis of the liability of the stockholder in such cases; and it follows that it is only those creditors who have relied, or who can fairly be presumed to have relied, upon the professed amount of capital, in whose favor the law will recognize and enforce an equity against the holders of 'bonus' stock. This furnishes a rational and uniform rule, to which familiar principles are easily applied, and which frees the subject from many of the difficulties and apparent inconsistencies into which the 'trust-fund' doctrine has involved it: and we think that even when the trust fund doctrine has been

<sup>393</sup> See the cases above cited. And see infra, this section, (j).

invoked, the decision in almost every well-considered case is readily referable to such a rule."394

(b) Issue of stock for cash at a discount.—The doctrine that the issue of watered or fictitiously paid up stock is a fraud upon persons who become creditors of the corporation in reliance upon its capital stock clearly applies when the original stock of a corporation is issued for cash as paid-up, under an agreement that payment in full shall not be required. Even in the absence of express statutory or constitutional provisions, as well as where there are such provisions, a court of equity, or other court having jurisdiction of winding-up proceedings. will disregard the agreement and enforce full payment for the stock so far as may be necessary to satisfy the claims of the creditors of the corporation who have dealt with it in reliance on the stock being full-paid; and by statute in some jurisdictions a creditor may proceed at law.395

When stock is issued to subscribers for less than its par value in cash, the right of creditors to compel full payment cannot be defeated by showing that there was no actual fraudulent intent in the transaction.396

(c) Issue of stock as a gratuity.—In a New York case, where a corporation had issued paid-up stock as a gratuity, it was held that a judgment creditor of the corporation, on its becoming insolvent, could not maintain a suit in equity to compel the stockholder to pay for the stock contrary to his agreement with the corporation. "The liability of a shareholder to

& Car Co., 48 Minn. 174, 31 Am. St. Rep. 637, 1 Cum. Cas. 885.

London Celluloid Co., 39 Ch. Div. other cases in note 386, supra. 190, 59 L. T. 109; Sagory v. Du-396 Flinn v. Bagley, 7 Fed. 785. 190, 59 L. T. 109; Sagory v. Du-

 

 394 Hospes v. Northwestern Mfg.
 bois, 3 Sandf. Ch. (N. Y.) 466;

 Car Co., 48 Minn. 174, 31 Am. St.
 Union Mut. Life Ins. Co. v. Frear

 ep. 637, 1 Cum. Cas. 885.
 Stone Mfg. Co., 97 Ill. 537, 37 Am.

 Rep. 129; Great Western Tel. Co. 395 Scovill v. Thayer, 105 U. S. v. Gray, 122 III. 630; Bates v. Great 143, 2 Keener's Cas. 897, 2 Smith's Western Tel. Co., 134 Ill. 536; Al-Cas. 818; Flinn v. Bagley, 7 Fed. ling v. Wenzel, 133 III. 264; Guer-785; Ooregum Gold Min. Co. v. ney v. Moore, 131 Mo. 650; Nenny Roper, [1892] App. Cas. 125, 66 L. v. Waddill, 6 Tex. Civ. App. 244; T. 427, 2 Cum. Cas. 247; Welton New Haven Trust Co. v. Gaffney, v. Saffery, [1897] App. Cas. 299; 73 Conn. 480; Bent v. Underdown, In re Addlestone Linoleum Co., 37 156 Ind. 516; Walter v. Merced Ch. Div. 191, 58 L. T. 428; In re Academy Ass'n, 126 Cal. 582; and

pay for his stock," said the court, "does not arise out of his relation, but depends upon his contract, express or implied, or upon some statute, and in the absence of either of these grounds of liability, we do not perceive how a person to whom shares have been issued as a gratuity has, by accepting them, committed any wrong upon creditors, or made himself liable to pay the nominal face of the shares as upon a subscription or contract."397 It does not appear, from the report of this case, whether the creditor was such when the stock was issued, or became such after it was issued, and in reliance on its being in fact full-paid. If the former, then the decision is clearly a sound one,398 but if the latter, it is contrary to the prevailing rule.

As we have seen, it is on the ground of fraud, and not on the ground of contract, that persons to whom stock has been issued as full-paid, when it is not so in fact, are held liable to creditors, and the reason for the doctrine, therefore, applies as well where stock is issued as a gratuity as where it is issued for cash at a discount. In the former case, the holder does not agree to pay anything; in the latter, he does not agree to pay anything further than what he has paid. It has repeatedly been held, therefore, that if a corporation issues its stock as full-paid without receiving any consideration, and particularly when it does so in violation of an express charter, statutory, or constitutional provision, and the stock is falsely held out to the public as being full-paid, the transaction, even when binding upon the corporation and consenting stockholders, operates as a fraud upon persons who subsequently deal with the corporation and become creditors on the faith of its capital stock being full-paid, and a court of equity, or, in some jurisdictions by statute, a court of law, will compel full payment for the stock, if necessary for the satisfaction of their claims. 399

<sup>&</sup>lt;sup>397</sup> Christensen v. Eno, 106 N. Y. 97, 60 Am. Rep. 429, 2 Keener's Pub. Co., 68 L. T. 649; Richardson Cas. 1240. See, also, Christensen v. Green, 133 U. S. 30; Handley v. V. Quintard, 8 N. Y. Supp. 400. Stutz, 139 U. S. 417, 2 Keener's Cas. 976, 2 Smith's Cas. 844, 1

In California it is held that where a certificate of stock is issued without any consideration, in violation of the statutory provision of that state that no corporation shall issue stock except for money, labor, or property actually received, and all fictitious increase of stock shall be void, the certificate is absolutely void for all purposes, and that the holder is not liable to creditors as for an unpaid subscription. 400 In some of the other states it is held otherwise.401

(d) Issue of stock for property, labor, or services.—If a corporation issues its stock as full-paid for property, labor, or services taken at an intentional overvaluation, the real value being less than the par value of the stock, the issue is just as truly an issue of the stock for less than its par value as if it were issued for cash at a discount, and in so far as the par value of the stock exceeds the value of the property, it is not in fact fully paid. The courts, however, have not agreed as to the right of creditors to compel the holders of such stock to pay the full par value.

In England, as was stated at the beginning of this section, it was held in the earlier cases that when stock is issued for property, labor, or services, taken at an overvaluation, so that the stock is not in fact fully paid for, the courts, while they may set the transaction aside, and place the parties in statu quo, cannot substitute a different agreement, and compel the stockholders, even for the purpose of paying the debts of the corporation, to pay the difference between the par value of the

Cum. Cas. 855, 41 Fed. 531; 49 La. Ann. 1350; Barto v. Nix, 15 Allen v. Fairbanks, 45 Fed. 445; Wash. 563; Hebberd v. Southwest-Hospes v. Northwestern Mfg. & ern Land & Cattle Co., 55 N. J. Car Co., 48 Minn. 174, 31 Am. Eq. 18. St. Rep. 637, 2 Keener's Cas. 1890, Comp. 1 Cum. Cas. 885; Hickling v. Wil- as to 1 son, 104 Ill. 54; Tuthill Spring Co. chasers of bonds. v. Smith, 90 Iowa, 331; Haldeman v. Ainslie, 82 Ky. 395; Peninsular Sav. Bank of Detroit v. Black Flag Stove Polish Co., 105 Mich. 535; 434, 76 Mo. 384; Belknap v. Adams, Skrainka v. Allen, 76 Mo. 384; Belknap v. Adams, Skrainka v. Allen, 76 Mo. 384; Belknap v. Adams, Skrainka v. Allen, 76 Mo. 384; Belknap v. Adams, Skrainka v. Allen, 76 Mo. 384; Belknap v. Adams, Ainclie 28 Kr. 205 Mo. App. 434; Belknap v. Adams. Ainslie, 82 Kv. 395.

Wash. 563; Hebberd v. Southwest-

Compare infra, this section, (g), as to bonus stock issued to pur-

stock and the actual value of the property, labor, or services. 402 In the later cases, however, under a statutory provision that every share in any company shall be deemed and taken to have been issued and to be held subject to the payment of the whole amount thereof in cash, unless the same shall have been otherwise determined by a contract duly made in writing, and registered, it has been held that, when shares have been issued for property or services at an intentional overvaluation, the stockholders, upon a winding up of the corporation, may be compelled to pay, for the benefit of creditors, the difference between the par value of the stock and the actual value of the property or services.403

In this country, although there are a few decisions apparently to the contrary, 404 it is settled in most jurisdictions that, if a corporation has issued its original stock as full-paid, taking in payment property, labor, or services at a fraudulent overvaluation, or in most states at an intentional overvaluation, whether there is an actual fraudulent intent or not, there is as clearly a fraud upon persons who have subsequently become creditors of the corporation in reliance upon the stock being fully paid for as if it had been issued for less than par in cash; and if the corporation is insolvent, the stockholders may, at the instance of such creditors, be compelled to pay the difference between the par value of the stock and the true value of the property or services. This doctrine has not only been applied under statutory or constitutional provisions regulating the issue of stock, but it has frequently been applied independently of any such provision.405

402 In re Great Northern & Midson's Case, 7 Ch. Div. 75,

408 In re Eddystone Marine Ins. Co., 68 L. T. 408, 69 L. T. 363.

404 See Phelan v. Hazard, 5 Dill. 45, Fed. Cas. No. 11,068; Van Cott v. Van Brunt, 82 N. Y. 535, 2 Keener's Cas. 954. As to these cases, see infra, this subsection.

405 United States: Camden v. land Coal Co., 3 De Gex, J. & S. Stuart, 144 U. S. 104; Northwest-367, 2 Smith's Cas. 817; Ander- ern Mut. Life Ins. Co. v. Cotton Exchange Real Estate Co., 46 Fed. 22, 70 Fed. 155.

Alabama: Elyton Land Co. v. Birmingham Warehouse & Elevator Co., 92 Ala. 407, 25 Am. St. Rep. 65, 1 Cum. Cas. 870.

Illinois: Coleman v. Howe, 154 III. 458, 45 Am. St. Rep. 133; World's

"If there is a fraudulent overvaluation of the property taken by the corporation for the stock," said the Illinois court, "the stockholder is liable for the difference between the actual value and the accepted value of such property, and consequently his stock is regarded as unpaid stock to the extent of that difference." 406

In a leading New Jersey case, five persons entered into a contract for the purchase of a tract of land for \$50,000, and or-

Fair E. & T. Boat Co. v. Gasch, 162 Ill. 402; Sprague v. National Bank of America, 172 Ill. 149, 64 Am. St. Rep. 17; National Bank of America v. Pacific Ry. Co., 66 Ill. App. 320.

Coffin v. Ransdell, 110 Indiana: Ind. 417; Bruner v. Brown, 139 Ind. 600; Clow v. Brown, 150 Ind.

Coffin v. Ransdell, supra, has sometimes been cited as contrary to this doctrine, but it is not so. It was merely held in that case that an action at law could not be maintained by a receiver of a corporation to collect as unpaid subscriptions the difference between the actual value of the property given by subscribers in payment for their stock and the par value of their stock, where there was no fraud. It was said that the trans-action might be impeached in equity for fraud.

Iowa: Osgood v. King, 42 Iowa, 478; Jackson v. Traer, 64 Iowa, 469, 52 Am. Rep. 449; Chisholm Bros. v. Forny, 65 Iowa, 333; Boulton Carbon Co. v. Mills, 78 Iowa, 460; Wishard v. Hansen, 99 Iowa, 307, 61 Am, St. Rep. 238; Stout v. Hub-

bell. 104 Iowa, 499.

Libby v. Tobey, 82 Me. Maine:

Crawford v. Rohrer, Maryland: 59 Md. 599; Brant v. Ehlen, 59

Michigan: Peninsular Sav. Bank of Detroit v. Black Flag Stove Polish Co., 105 Mich. 535.

Minnesota: Hastings Malting Co. v. Iron Range Brewing Co., 65 Minn. 28, 2 Smith's Cas. 831; Wal- 471, 45 Am. St. Rep. 133, 137.

lace v. Carpenter Electric Heating Mfg. Co., 70 Minn. 321, 68 Am. St. Rep. 530.

Missouri: Van Cleve v. Berkey, 143 Mo. 109; Shickle v. Watts, 94 Mo. 410, qualified to some extent in Woolfolk v. January, 131 Mo.

Kelly v. Fourth of Montana: July Min. Co., 21 Mont. 291.

Nebraska: Gilkie & Anson Co. v. Dawson Town & Gas Co., 46 Neb.

New Jersey: Wetherbee v. Baker, 35 N. J. Eq. 501; Hebberd v. Southwestern Land & Cattle Co., 55 N. J. Eq. 18; Lee v. Heppenheimer, 55 N. J. Eq. 240.

North Carolina: Clayton v. Ore Knob Co., 109 N. C. 385. Ohio: Gates v. Tippecanoe Stone Co., 57 Ohio St. 60. Kelley

Tennessee: Fletcher, 94 Tenn. 1, 6.

Utah: Henderson v. Turngren, 9 Utah, 432; Salt Lake Hardware Co. v. Tintic Milling Co., 13 Utah,

Virginia: Martin v. South Salem Land Co., 94 Va. 28.

Manhattan Trust Washington: Co. of New York v. Seattle Coal & Iron Co., 16 Wash. 499; Adamant Mfg. Co. of America v. Wallace, 16 Wash. 614; Kroenert v. Johnston, 19 Wash. 96; Dunlap v. Rauch (Wash.) 64 Pac. 807.

Wisconsin: Gogebic Inv. Co. v. Iron Chief Min. Co., 78 Wis. 427, 23 Am. St. Rep. 417; National Bank of Merrill v. Illinois & Wisconsin Lumber Co., 101 Wis. 247. 406 Coleman v. Howe, 154 Ill. 458,

ganized a corporation to take the same. In the certificate of incorporation the capital stock was fixed at \$100,000, and these persons subscribed for the whole of it, and became the directors. The deed for the land was made directly to the corporation, and it gave its obligations for the whole purchase money. The directors then appraised the land at \$100,000, although it was not worth more than the purchase price of \$50,000, and credited \$50,000 of the valuation as a payment on the subscriptions to the capital stock. In a suit by a creditor of the corporation it was held that, as against creditors, the allowance of the credit on subscriptions was invalid, and the stockholders were required to pay the subscriptions in full.<sup>407</sup>

When stock is issued to a subscriber for property taken at an overvaluation, the fact that the subscription is cancelled, and the stock issued in form as upon a purchase of the property, does not prevent the court from holding the subscriber liable for the difference between the par value of the stock and the actual value of the property.<sup>408</sup>

In the absence of a statute, the remedy of a creditor is in equity, but by statute in some jurisdictions he is allowed to maintain an action at law directly against the stockholder.<sup>409</sup>

Cases apparently to the contrary.—In a federal case decided by Judges Dillon and Treat in 1878, suit was brought by a creditor of a corporation to charge a transferee of stock, who had purchased the same in good faith and for value as full-paid, on the ground that it was paid for in property at an overvaluation. It was held, principally on the authority of the earlier English cases, that no liability could be established against the defendant by showing that the property conveyed to the corporation in payment for the stock was not worth the amount of the stock, or that it was not worth anything over and above mortgages which covered it at the time of the trans-

<sup>407</sup> Wetherbee v. Baker, 35 N. J.

408 Hebberd v. Southwestern Land

& Cattle Co., 55 N. J. Eq. 18.

409 See infra, this section, (1).

fer. The decision was put upon the ground that the agreement under which the property was received in payment for the stock was conclusive upon the corporation and its creditors, unless impeached and rescinded in a direct attack on the ground of fraud, and it was said that "the courts, even where the rights of creditors are involved, will treat that as a payment which the parties have agreed should be payment." 410

In a New York case it appeared that the defendant, who was the president and a director of a railroad company, as such entered into a contract with a third person, by which the latter agreed to build and equip a portion of the road, for a certain sum in stock of the company, and for a certain sum in its bonds; and immediately afterwards, in accordance with a previous arrangement, the contract was assigned to the defendant, who, with others associated with him, performed the contract at an expense less than the par of the stock and bonds agreed to be paid therefor, and which the defendant and his associates received. It appeared, however, that the contract was entered into and assignment made in good faith, after full deliberation and consultation, with the knowledge and consent of all the directors and stockholders of the company, as the only means to insure the construction of the road, and that the amount expended in the performance of the contract exceeded the actual value of the stock and bonds delivered in payment. Under these circumstances, it was held that the defendant was not liable, at the suit of a receiver of the company, for the difference between the par value of the stock received by him and the cost of his performance of the contract.411 not appear from the report of this case whether the creditors for whom it was sought to compel payment became so after the stock was issued, or before, or whether they were in any way deceived by the issue of the stock for less than its par value. If they were existing creditors at the time the stock was issued, or if, though they became so afterwards, they knew of the

<sup>410</sup> Phelan v. Hazard, 5 Dill. 45, 411 Van Cott v. Van Brunt, 82 N. Fed. Cas. No. 11,068. Y. 535, 2 Keener's Cas. 954.

circumstances, they were not in any way injured, and the decision was right, for only those creditors who have dealt with the corporation after the issue of fictitiously paid up stock, and upon the faith of its being paid up, can complain.412 the court meant to hold, as the dicta of the court would seem to imply, that persons who take original capital stock of a corporation at less than its par value, either in money, or in property intentionally overvalued, are not liable to subsequent creditors who deal with the corporation on the faith of its capital stock, the decision is opposed to the overwhelming weight of authority.413

- (e) Valuation of the property.—In order that creditors may hold stockholders liable who have paid for their stock in property, on the ground that the property was overvalued, the overvaluation must have been fraudulent, or at least intentional. In some states it must have been fraudulent in fact.414 the valuation was made in good faith, and the overvaluation was due to mistake or error of judgment, there is no liability even to creditors.415 The question of overvaluation of property has been considered at length in a former section.416
- (f) Loans to stockholders.—Although a corporation may contract with its stockholders, and lend them money if it acts in good faith and without prejudice to the rights of creditors, it cannot resort to any such a device for the purpose of relieving them from payment for their shares, to the injury of creditors. It was held, therefore, in a leading case in the supreme court of the United States, that an arrangement by which the stock of a corporation was nominally paid for by the subscribers, and the money was immediately repaid as a loan to them, was a

<sup>412</sup> See infra, this section, (j). 413 See 2 Morawetz, Corp. § 826; Taylor, Corp. § 522(c), page 524, note; Elyton Land Co. v. Birmingham Warehouse & Elevator Co., 92

<sup>414</sup> Ante, § 392.

<sup>415</sup> Coit v. Gold Amalgamating Co., 119 U. S. 343, 2 Smith's Cas. 839, 2 Keener's Cas. 1887, 1 Cum. Cas. 847; Bank of Fort Madison v. Alden, 129 U.S. 372; Woolfolk v. Ala. 407, 25 Am. St. Rep. 65, 1 January, 131 Mo. 620; Bickley v. Cum. Cas. 870. Schlag, 46 N. J. Eq. 533. 416 Ante, § 392.

mere device to change the subscribers' indebtedness from a stock debt to a loan, and was not a valid payment, as against creditors of the corporation.417

(g) Issue of additional stock after organization of corporation. -The doctrine under which stockholders of a corporation are held liable to pay the full amount of their stock for the benefit of creditors, notwithstanding an agreement to the contrary with the corporation, is not limited to original capital stock, but applies also, subject to some limitations, to new stock issued by a corporation upon increasing its capital stock. If a corporation increases its capital stock for the mere purpose of adding to the original capital stock, and enabling it to do a larger and more profitable business, a subscriber for the new stock is in substantially the same position as a subscriber for the original stock, in so far as payment therefor is concerned If the stock is issued as full-paid, upon payment or agreement to pay in part only, or gratuitously, and the corporation becomes insolvent, subsequent bona fide creditors may compel him to pay the balance, if necessary for the satisfaction of their claims, as shown in the preceding paragraphs.418

By the weight of authority, however, there is no such liability, in the absence of a statute, where an active corporation becomes embarrassed and issues an increase of its capital stock in good faith at the best price that can be obtained, although it may be less than the par value, either in the payment of debts, or to raise money for the successful continuance of its business: 419 or where it issues such stock in good faith as a

Creditors of a corporation are presumed to have trusted it on the 2 Keener's Cas. 967; Fogg v. Blair, faith of an increase in the capital 139 U. S. 118; Handley v. Stutz.

S.) 610, 2 Smith's Cas. 812.

<sup>531;</sup> Flinn v. Bagley, 7 Fed. 785, 1 Cum. Cas. 845; Rickerson Roller-Mill Co. v. Farrell Foundry & Machine Co. (C. C. A.) 75 Fed. 554.

<sup>417</sup> Sawyer v. Hoag, 17 Wall. (U. stock from the time it was voted. and the fact that subscribers there-418 Handley v. Stutz, 139 U. S. for did not receive it until after 417, 2 Keener's Cas. 976, 2 Smith's the debts were contracted will not Cas. 844, 1 Cum. Cas. 855, 41 Fed. relieve them from liability in case the stock is not in fact full-paid. Handley v. Stutz, 139 U. S. 417, 2 Keener's Cas. 967, 2 Smith's Cas. 844, 1 Cum. Cas. 855,

bonus in order to induce persons to purchase its bonds at their par value. 420 The transaction must be in good faith, and not a mere device for recklessly or fraudulently disposing of the stock to the prejudice of stockholders or creditors. 421

In a case in the supreme court of the United States, a railroad company, being indebted to a construction company in the sum of \$70,000, which it was unable to pay in money, had a settlement with the construction company, whereby the debt was paid in shares of the stock of the railroad company of the par value of \$350,000, the stock being taken at twenty cents on the dollar, but not being worth at the time anything at all on the market. It was held that the issue of the stock was not a fraud upon subsequent creditors, nor ultra vires, so as to render the members of the construction company, among whom it was distributed, liable upon the same as unpaid stock, and that they could not be held liable under a statute merely imposing liability to the amount of unpaid installments on stock. 422

In another case in the supreme court of the United States, a corporation issued new stock as a bonus to purchasers of its bonds in order to dispose of the bonds, and the transaction was upheld as against creditors. "To say," said Mr. Justice Brown, "that a corporation may not, under the circumstances above indicated, put its stock upon the market and sell it to the high-

139 U. S. 417, 2 Keener's Cas. 976, Where suit was brought against 2 Smith's Cas. 844, 1 Cum. Cas. contractors for the building of a 855; Dummer v. Smedley, 110 Mich. railroad to hold them liable for the 466; Stein v. Howard, 65 Cal. 616, face value of stock received by ham, 1 Tex. Civ. App. 58.

420 Fogg v. Blair, 139 U. S. 118; Smedley, 110 Mich. 466.

422 Clark v. Bever, 139 U. S. 96, U. S. 118.

2 Keener's Cas. 967.

2 Keener's Cas. 963; Kellerman v. them in payment for work done, Maier, 116 Cal. 416; Mathis v. Pridand the bill alleged that they got \$12,000 in the company's first-mort-Contra, Jackson v. Traer, 64 gage bonds for each mile of con-Iowa, 469, 52 Am. Rep. 449. structed road, and in addition \$850,000 in stock, and that the Handley v. Stutz, 139 U. S. 417, 2 bonds were full and adequate com-Keener's Cas. 976, 2 Smith's Cas. pensation for the work, but which 844, 1 Cum. Cas. 855; Dummer v. contained no allegation as to the real value of the stock, it was held 421 Fogg v. Blair, 139 U. S. 118. that the bill was bad on demurrer, See New Castle & Northwestern for not showing that the stock was Ry. Co. v. Simpson, 21 Fed. 533. of some value. Fogg v. Blair, 139 est bidder, is practically to declare that a corporation can never increase its capital by a sale of shares, if the original stock has fallen below par. The wholesome doctrine, so many times enforced by this court, that the capital stock of an insolvent corporation is a trust fund for the payment of its debts, rests upon the idea that the creditors have a right to rely upon the fact that the subscribers to such stock have put into the treasury of the corporation, in some form, the amount represented by it; but it does not follow that every creditor has a right to trace each share of stock issued by such corporation, and inquire whether its holder, or the person of whom he purchased, has paid its par value for it. It frequently happens that corporations, as well as individuals, find it necessary to increase their capital in order to raise money to prosecute their business successfully, and one of the most frequent methods resorted to is that of issuing new shares of stock and putting them upon the market for the best price that can be obtained; and so long as the transaction is bona fide, and not a mere cover for 'watering' the stock, and the consideration obtained represents the actual value of such stock, the courts have shown no disposition to disturb it. Of course no one would take stock so issued at a greater price than the original stock could be purchased for, and hence the ability to negotiate the stock and to raise the money must depend upon the fact whether the purchaser shall or shall not be called upon to respond for its par value. While, as before observed, the precise question has never been raised in this court, there are numerous decisions to the effect that the general rule that holders of stock, in favor of creditors, must respond for its par value, is subject to exceptions where the transaction is not a mere cover for an illegal The liability of a subscriber for the par value of increased stock taken by him may depend somewhat upon the circumstances under which, and the purposes for which, such increase was made. If it be merely for the purpose of adding to the original capital stock of the corporation, and enabling it to do a larger and more profitable business, such subscriber would stand practically upon the same basis as a subscriber to the original capital. But we think that an active corporation may, for the purpose of paying its debts, and obtaining money for the successful prosecution of its business, issue its stock and dispose of it for the best price that can be obtained."<sup>1423</sup>

(h) Stock issued and reacquired by the corporation.—It is too clear to admit of question, that, when stock has been once issued and fully paid for, there is nothing to prevent the stockholders from returning the whole or a part thereof to the corporation, or to a trustee for its use, to be disposed of for its benefit; and in such a case the corporation or trustee may dispose of the stock at less than its par value without violating statutory or constitutional provisions regulating the issue of stock, and without rendering purchasers thereof liable to creditors beyond the price which they agree to pay.<sup>424</sup>

When stock which has been subscribed, paid for in full, and issued, is by the holders thereof placed in the hands of a trustee to be paid over to subscribers for bonds of the corporation, when their subscriptions to such bonds are paid in full, such stock may lawfully be transferred by the trustee to the subscribers for bonds, upon payment of their subscriptions, without violating the constitutional or statutory provision that stock or bonds shall not be issued except for money paid, labor done, or property actually received, and that all fictitious increase of stock or indebtedness shall be void. And the failure to pay their subscriptions for bonds does not make such subscribers liable upon the stock agreed to be delivered, as upon unpaid subscriptions for stock<sup>425</sup>

Stock acquired by forfeiture or purchase.—The same is true of stock which has been lawfully issued by a corporation, and

<sup>423</sup> Handley v. Stutz, 139 U. S. 127; Lake Superior Iron Co. v. 417, 2 Keener's Cas. 976, 2 Smith's Drexel, 90 N. Y. 87. Compare Al-Cas. 844, 1 Cum. Cas. 855, followed ling v. Wenzel, 133 III. 264. in Dummer v. Smedley, 110 Mich.

466.

425 Davis Bros. v. Montgomery

<sup>424</sup> Davis Bros. v. Montgomery Furnace & Chemical Co., 101 Ala. Furnace & Chemical Co., 101 Ala. 127.

afterwards reacquired by it by forfeiture for nonpayment of assessments thereon, or by a valid purchase. It holds such stock as it holds other assets, and may lawfully sell the same at its market price, although it may be less than the par value, without rendering the purchasers liable to creditors. 426

This exception to the general doctrine does not apply where the transaction under which the corporation reacquires the shares is not in good faith, but a mere device on the part of the stockholders to avoid payment in full. Stockholders cannot escape liability to creditors by subscribing for stock, and then surrendering it to the corporation before payment therefor, and afterwards taking the same from the corporation, controlled by them, at a reduced value.<sup>427</sup>

(i) Extent of liability.—The holders of watered or fictitiously paid up stock are liable, for the benefit of creditors of the corporation, to such an extent only as may be necessary for the satisfaction of their claims. When the assets of a corporation are abundantly sufficient for the payment of the debts of the corporation, and have, either by law or by act of the corporation, been set apart and secured primarily for that purpose, stockholders cannot be required to pay up anything due on their subscriptions. 429

Where stock is issued for property of equal value, and it is afterwards ascertained that the vendor had no title to a fractional part of the property, and the corporation purchases it from the true owner, the vendor is liable, not for the amount so paid by the corporation, but for the difference between the value of the property to which he had title and the face value of the stock at the time the stock was issued to him.\*

<sup>426</sup> Ramwell's Case, 50 L. J. Ch. 827; Otter v. Brevoort Petroleum Co., 50 Barb. (N. Y.) 427; Chillicothe Branch of State Bank of Ohio v. Fox, 3 Blatchf. 431, Fed. Cas. No. 2,683; Pullman v. Railway Equipment Co., 73 III. App. 313.
427 Alling v. Wenzel, 133 III. 264.

<sup>427</sup> Alling v. Wenzel, 133 Ill. 264. See, also, Belknap v. Adams, 49 La. Ann. 1350.

<sup>428</sup> See Scovill v. Thayer, 105 U. S. 143, 2 Keener's Cas. 897, 2 Smith's Cas. 818.

<sup>429</sup> Albitztigui v. Guadalupe, etc., Min. Co., 92 Tenn. 598. See post, chapter xxv.

<sup>\*</sup>Jenkins v. Bradley, 104 Wis. 540

(j) Existing creditors, and creditors participating, consenting, or with knowledge.—As we have seen, the doctrine that persons who receive stock of a corporation under an agreement by which they are to pay nothing therefor, or to pay less than its par value, may be compelled to pay in full for the benefit of creditors of the corporation, is based upon the ground of fraud.430 It can be invoked, therefore, in favor of such creditors only as have dealt with the corporation on the faith of the stock being fully paid. Those who have not done so are not defrauded, and cannot complain. "The whole doctrine that the capital stock of corporations is a trust fund for the payment of creditors," said the Minnesota court in a late case, "rests upon the equitable consideration that the distribution of the capital among stockholders without making adequate provision for the payment of debts, or the issue of fictitiously paid up stock, is a fraud upon creditors who contract with the corporation in reliance upon its capital remaining intact, or in reliance upon the professed capital having been in fact paid up in full. But when the reason for the rule does not exist the rule itself ceases to apply. This trust does not arise absolutely in every case, in favor of every and any creditor. It is not true, and no case can be found which holds, that it is in the power of a creditor in every and all cases, as a matter of right, to institute an inquiry as to the value 'or amount of the consideration given for stock issued as fully paid up, any more than that it would be his right, in any and every case, to inquire into the distribution of the capital among the shareholders. It is only those creditors who can fairly allege that they have relied, or whom the law presumes to have relied, upon the amount of capital stock of the company, who have a right to make such inquiry, or in whose favor equity will impress a trust upon the subscription to the stock, and set aside a fictitious arrangement for its payment."431

It follows that an issue of watered or fictitiously paid up

<sup>480</sup> Supra, this section, (a). Min. Co., 42 Minn. 327, 18 Am. St.
481 First Nat. Bank of Deadwood Rep. 510, 2 Smith's Cas. 835, 1
v. Gustin Minerva Consolidated Cum. Cas. 850.

stock by a corporation cannot be attacked, nor the holders thereof be compelled to pay its full par value, by or for the benefit of persons who dealt with the corporation and became creditors before the stock was issued. 432 The same is true of a creditor who participated in the issue of the stock, or consented thereto, whether he participated as a stockholder or officer of the corporation, or as its attorney, or otherwise. 433 And it is equally

Nat. Bank of Deadwood v. Gustin Minerva Consolidated Min. Co., 42 Minn. 327, 18 Am. St. Rep. 510, 2 Smith's Cas. 835, 1 Cum. Cas. 850; Hospes v. Northwestern Mfg. & Car Co., 48 Minn. 174, 31 Am. St. Rep. creditors who were stockholders, 637, 2 Keener's Cas. 1890, 1 Cum. and had notice of an agreement for Cas. 885. See, also, Graham v. the issue of stock at less than par, Railroad Co., 102 U. S. 148, 1 Cum. could not demand from the sub-Cas. 1006.

unpaid stock, whenever subscribed, pay and the face of the stock, and is a trust fund for the payment of that they had no right to particiall corporate debts, whether creat- pate in the fund contributed by ed before or subsequent to the sub- the subscribers to pay creditors not scriptions. Shields v. Clifton Hill having such notice. Land Co., 94 Tenn. 123, 45 Am. St. Pridham, 1 Tex. Civ. App. 58. Rep. 700.

Where a creditor otherwise

Rep. 700.

428 Bank of Fort Madison v. Alden, 129 U. S. 372; Coit v. Gold Amalgamating Co., 119 U. S. 343, 2 Smith's Cas. 839, 1 Cum. Cas. 847; Rickerson Roller-Mill Co. v. Farrell Foundry & Machine Co. (C. C. A.) 75 Fed. 554; Nicrosi v. Calera Land Co., 115 Ala. 429; Ten Eyck v. Pontiac, Oxford & P. A. R. Co., 114 Mich. 494; Callanan v. Windsor, 78 Iowa, 193; Ambler v. Archer, 1 App. D. C. 94; Knoop v. Bohmrich, 49 N. J. Eq. 82.

Where certain persons purchased

432 Handley v. Stutz, 139 U.S. for every dollar paid to the fund 417, 2 Keener's Cas. 976, 2 Smith's for purchasing the land, which was Cas. 844, 1 Cum. Cas. 855, affirming done, it was held that one of such Stutz v. Handley, 41 Fed. 531; Con- persons, who became a director of tinental Trust Co. v. Toledo, St. the corporation, and afterwards Louis & K. C. R. Co., 82 Fed. 642; sold his stock and became a cred-Coit v. Gold Amalgamating Co., 14 itor, could not, on its becoming in-Fed. 12, 119 U. S. 343, 2 Keener's solvent, maintain a bill to compel Cas. 839, 1 Cum. Cas. 847; First the other subscribers to pay the difference between the face value of their stock and the value of the Nicrosi property conveyed. Calera Land Co., 115 Ala. 429.

In a Texas case it was held that as. 1006. scribers that they pay the differ-Under a statute in Tennessee, all ence between what they agreed to Mathis

Where certain persons purchased ment of a claim against a corporaand to be conveyed to a corpora-tion, after it has issued stock for tion to be afterwards formed, and less than its par value, is not which was to issue them stock at precluded from enforcing the lia-the rate of five dollars of stock bility of stockholders for the baltrue of a creditor who dealt with the corporation with actual or constructive notice of the circumstances under which the stock was issued.434

In Illinois, the rule is different. In that state a statute provides that "each stockholder shall be liable for the debts of the corporation to the extent of the amount that may be unpaid the stock held by him," and it has been held that the right of a creditor to compel a stockholder to pay the difference between the par value of his stock and what he has paid in money. or property under his agreement with the company is not in any way affected by the fact that he knew, or did not know,

his assignor was a stockholder. Montgomery v. Brush Electric Iltuminating Co., 48 App. Div. (N. Y.) 12, affirmed 168 N. Y., mem.

434 Coit v. Gold Amalgamating Co., 119 U. S. 343, 2 Keener's Cas. 1887, 2 Smith's Cas. 839, 1 Cum. (as. 847; Kenton Furnace Railroad & Mfg. Co. v. McAlpin, 5 Fed. 737; Northwestern Mut. Life Ins. Co. v. Cotton Exchange Real Estate Co., 70 Fed. 155; Rickerson Roller-Mill Co. v. Farrell Foundry & Machine Where the promoters of a corpo-Co. (C. C. A.) 75 Fed. 554; First ration agreed to purchase land at Nat. Bank of Deadwood v. Gustin Minerva Consolidated Min. Co., 42 Minn. 327, 18 Am. St. Rep. 510, 2 Smith's Cas. 835, 1 Cum. Cas. 850; Hospes v. Northwestern Mfg. & Car America v. Wallace, 16 Wash. 614; Whitehill v. Jacobs, 75 Wis. 474; Walburn v. Chenault, 43 Kan. 352; Callanan v. Windsor, 78 Iowa, 193.

a corporation expressly provide that only a certain per cent. of is not an asset for the benefit of 333.

ance on the stock by the fact that creditors of the corporation on its becoming insolvent, since the articles give notice of the liability of the stockholders. Bent v. Underdown, 156 Ind. 516.

The record of incorporation proceedings is not constructive notice to subsequent creditors of the real value of property received in payment of subscriptions to stock, or that it was grossly overvalued. Lea v. Iron Belt Mercantile Co., 119 Ala. 271.

a grossly excessive valuation, and issue the stock of the corporation in payment, and the articles of incorporation recited the contract, and that the directors should pay Co., 48 Mins. 174, 31 Am. St. Rep. for the land by issuing stock at par 637, 2 Keener's Cas. 1890, 1 Cum. for the agreed valuation, and that Cas. 885; Woolfolk v. January, 131 the stock, when so issued, should Mo. 620; Adamant Mfg. Co. of be held and regarded as fully paid for by the conveyance of the land to the corporation, it was held that the articles were not notice to subsequent creditors that the land had Where the recorded articles of been overvalued. Stout v. Hubbell. 104 Iowa, 499.

Entries contained in the private the par value of the stock shall be books of a corporation are not nocollected except by unanimous con-tice to persons becoming creditors sent of the stockholders, and show of the corporation as to the way in the amount subscribed by each which stockholders have paid for stockholder, and the cash paid, the their shares. Gilkie & Anson Co. unpaid portion of the subscriptions v. Dawson Town & Gas Co., 46 Neb. when he extended credit to the company, that the stock was in part unpaid. The soundness of this decision, however, may well be doubted.

A creditor cannot enforce further payment by stockholders who have received watered or fictitiously paid up stock, if he has waived the right to do so by a special contract.<sup>436</sup>

(k) Effect of transfer.—The holder of watered or fictitiously paid up stock cannot escape liability to creditors by transferring the same to an irresponsible person or to a *bona fide* purchaser, and in some states he remains liable under all circumstances.<sup>437</sup>

Whether there is any liability on the part of the transferee depends upon whether he was a bona fide purchaser. If he purchased with notice, actual or constructive, that the stock was not in fact fully paid up, he is subject to the same liability as his transferrer; but he is not liable at all if he purchased without such notice.<sup>438</sup>

(1) Remedy of creditors.—In the absence of a statute, the remedy of creditors of a corporation to compel payment by holders of watered or fictitiously paid up stock is in equity, and he cannot, nor can a receiver, maintain an action at law directly against the stockholders.<sup>439</sup> In some jurisdictions, however,

435 Sprague v. National Bank of America, 172 Ill. 149, 168, 64 Am. St. Rep. 17, 32. "The liability of the stockholder," said the court in this case, "is established by the statute for the purpose of securing to the creditor the benefit of the entire fund which, in the contemplation of the statute, will be created by subscriptions to the capital stock of the corporation. The right of a creditor to avail himself of this liability of a stockholder arises out of the fact the stockholder has not, as the statute requires, paid the full amount of his subscription to the capital stock of the corporation, and the right is in no wise impaired by the fact that the creditor knew, or did not know, the stockholder was in default."

436 Bush v. Robinson, 95 Ky. 492. And see post, chapter xxv.

437 Wishard v. Hansen, 99 Iowa, 307, 61 Am. St. Rep. 238; Sprague v. National Bank of America, 172 Ill. 149, 64 Am. St. Rep. 17; White v. Greene (Iowa) 70 N. W. 182. And see post, chapter xxiii.

V. Greene (10wa) 70 N. W. 182. And see post, chapter xxiii.

\*\*3\* Steacy v. Little Rock & Ft. Smith R. Co., 5 Dill. 348, Fed. Cas. No. 13,329, 2 Smith's Cas. 869; Brant v. Ehlen, 59 Md. 1; Coleman v. Howe, 154 III. 458, 45 Am. St. Rep. 133; Young v. Erie Iron Co., 65 Mich. 111; Wallace v. Carpenter Electric Heating Mfg. Co., 70 Minn. 321, 68 Am. St. Rep. 530; West Nashville Planing-Mill Co. v. Nashville Sav. Bank, 86 Tenn. 252, 6 Am. St. Rep. 835, 2 Keener's Cas. 1233; Wishard v. Hansen, 99 Iowa, 307, 61 Am. St. Rep. 238. And see post, chapter xxiii.

v. Peavey, 69 Fed. 455; Thomson-

there are statutes which allow a creditor in such a case to maintain an action at law against a stockholder, or to levy an execution under a judgment against the corporation.440

### IV. ASSESSMENTS UPON STOCKHOLDERS OR MEMBERS AFTER PAYMENT IN FULL.

§ 402. In general.—A corporation cannot levy an assessment upon the holders of full-paid stock, or, in the case of nonstock corporations, upon members who have paid all that is required by their contract of membership, unless the power to do so is conferred by the charter or articles of association or a valid statute, or by consent of the stockholders or members; and the legislature cannot authorize such an assessment, without the consent of the stockholders or members, by a statute passed after their rights are acquired, unless the power to alter, amend, or repeal the charter has been reserved.

We shall consider in subsequent chapters the right of a corporation to make calls or assessments upon unpaid subscriptions to their capital stock,441 the rights of creditors with respect to unpaid subscriptions,442 and assessments upon stockholders for the payment of debts of an insolvent corporation under the statutes imposing liability over and above the par value of their shares.443 We have already considered the rights and liabilities arising out of the issue of watered or fictitiously paid up stock,—that is, stock issued as paid up, when it is not full-paid in fact.444 In this subdivision we shall consider the liability of stockholders to calls or assessments upon their shares after they have been in fact fully paid up (aside from the liability under statutes imposing liability for the benefit of creditors), and the right of nonstock corporations to levy assessments over

solidated Traction Ry. Co. (C. C. A.) 54 Fed. 1001; Coffin v. Ransdell, 110 Ind. 417. See post, chapter xxiii.

440 National Park Bank v. Peavey, 64 Fed. 912 (under the Iowa statute); Chisholm Bros. v. Forny,

Houston Electric Co. v. Dallas Con- 65 Iowa, 333; Libby v. Tobey, 82 Me. 397; Barron v. Burrill, 86 Me. 66. See post, chapter xxv.

<sup>441</sup> Post, § 497 et seq.

<sup>442</sup> Post, chapter xxv.

<sup>448</sup> Post, chapter xxv.

<sup>444</sup> Ante, § 389 et seq.

and above the amount which the members have agreed to contribute.

# § 403. Right to levy assessments.

It may happen that, when stockholders or members of a corporation have paid in full into the treasury of the corporation their required contributions to its capital stock or capital, so that their shares or membership are paid for in full, the corporation may have need of further funds. In such a case, the stockholders or members may undoubtedly contribute any additional sums they may choose, 445 although the capital stock of a corporation cannot be increased without legislative authority.446 It is well settled, however, that stockholders cannot be compelled to do so, unless additional liability is imposed by statute, or by the charter or articles of association. In the absence of a valid charter or statutory provision therefor, or an express agreement binding upon the stockholders, neither the board of directors nor a majority of the stockholders can levy and collect an assessment upon shares of stock which are fully paid for, whether the assessment is sought to be made for the purpose of raising money needed for the operations of the corporation, or for the purpose of paying its debts.447 And in the case of nonstock

the stockholders. See Bidwell v. Pittsburgh, Oakland & E. L. P. Ry. Utah, 265.

Portland R. Co. v. Kendall, 31 Me. Starch Co. v. Moore, 62 N. H. 671; 368; Salt Lake City Nat. Bank v. Gresham v. Island City Sav. Bank, Hendrickson, 40 N. J. Law, 52; 2 Tex. Civ. App. 52; Atlantic De Toney v. Fulkerson, 125 Ind. 224;

445 Such contributions become as- Laine Co. v. Mason, 5 R. I. 463; sets of the corporation, and do not State v. Morristown Fire Ass'n, 23 create debts against it in favor of N. J. Law, 195, 1 Keener's Cas. 845; Trustees of Free Schools in South Parish in Andover v. Flint, 13 Metc. Co., 114 Pa. St. 535; Leavitt v. Ox- (Mass.) 539; Wells v. Green Bay ford & Geneva Silver Min. Co., 3 & Mississippi Canal Co., 90 Wis. 442; John R. Proctor Land Co. v. 446 Ante, § 405 et seq.

447 Enterprise Ditch Co. v. Mof- van County Club v. Butter, 20 million fitt, 58 Neb. 642, 76 Am. St. Rep. Rep. (N. Y.) 306; Louisiana Paper Library Ass'n v. Co. v. Waples, 3 Woods, 34, Fed. Connell, 55 Neb. 396; Kennebec & Cas. No. 8,540; Smith v. Huckabee, 53 Ala. 191; Spense v. Iowa Val-470; Moore v. New Jersey Lighter- lev Construction Co., 36 Iowa, 407; age Co., 57 N. Y. Super. Ct. 1; Du- Gary v. York Min. Co., 9 Utah, 464; luth Club v. MacDonald, 74 Minn. Jones v. Jarman, 34 Ark. 323; My-254, 73 Am. St. Rep. 344; Lancaster ers v. Irwin, 2 Serg. & R. (Pa.) Starch Co. v. Moore, 62 N. H. 671; 368; Salt Lake City Nat. Bank v.

corporations, such as social clubs, boards of trade, and the like, when a member has contributed and paid all that the charter or articles of association require him to pay, he cannot be compelled to pay any further assessments, however much the additional funds may be needed.448

The power to assess paid-up stock, unless otherwise conferred, cannot be given, as against dissenting stockholders, by a by-law passed by a majority of the stockholders. "To hold that a bylaw imposing an annual assessment on stock already fully paid for is a lawful exercise of corporate power is tantamount to holding that a corporation may, by a single resolve, in the form of a by-law, put its stockholders in debt to it annually to any amount that it may see fit to specify, and all without their consent. To state such a proposition is simply to refute its legality."449

If a corporation levies an assessment without authority to do so, and undertakes to forfeit shares for nonpayment, the stockholder may sue to enjoin the forfeiture, or, if the shares have been forfeited, he may sue to recover damages for the conversion of his stock, and recover the value thereof. 450 ber has been expelled from-a nonstock corporation for nonpayment of an illegal assessment, he may in most jurisdictions in-

Redkey Citizens' Natural Gas, Light, Fuel & Petroleum Co. v. Orr (Ind. App.) 60 N. E. 716. And see post, chapter xxv., as to liability for debts.

Unless the liability is imposed by some statute or by an express agreement, stockholders who have paid in full for their shares, in money or property, are not liable to an assessment for the purpose of reimbursing officers of the corporation for money paid by them as officers of the company. John R. Procter Land Co. v. Cooke, 19 Ky. Law Rep. 1734.

448 Duluth Club v. MacDonald, 74 Minn. 254, 73 Am. St. Rep. 344; And see ante, § 379; post, § 495.

Citizens' Natural Gas, Omaha Law Library Ass'n v. Connell, 55 Neb. 396.

449 Sullivan County Club v. But-ler, 26 Misc. Rep. (N. Y.) 306. See, also, Hibernia Fire Engine Co. v. Com., 93 Pa. St. 264. Compare Omaha Law Library Ass'n v. Connell, 55 Neb. 396, wherein it was held that the charter of a corporation, which in one article authorized cancellation of a stockholder's stock for nonpayment of dues, and in another authorized it to make by-laws consistent with the various articles, authorized a by-law imposing annual dues upon the stockbolders.

450 Moore v. New Jersey Lighterage Co., 57 N. Y. Super. Ct. 1.

stitute mandamus proceedings to compel his reinstatement, or in some jurisdictions resort to other remedies.<sup>451</sup>

A stockholder or member of a corporation is not estopped to object to an assessment because previous unauthorized assessments have been paid. 452

## § 404. Power conferred by charter, statute, or agreement.

When neither the statutes of the state nor the charter or articles of association of a corporation, at the time persons become stockholders or members thereof, permit the corporation to levy assessments upon them over and above the amount of their shares or the amount agreed to be paid, as the case may be, the legislature cannot afterwards confer the power to levy such assessments, as against a dissenting stockholder or member, unless the power to alter, amend, or repeal the charter has been reserved, for such a statute would be unconstitutional as impairing the obligation of his contract with the corporation.453 The contrary has been held where the power to alter, amend, or repeal the charter has been reserved. 454 And of course liability to assessment may be imposed by a statute in force at the time the corporation is formed, or by its charter, or by the articles of association, or otherwise by agreement at the time of becoming a member or stockholder, or afterwards. 455

451 Ante, § 373(d).

452 Atlantic De Laine Co. v. Mason, 5 R. I. 463.

453 Enterprise Ditch Co. v. Moffit, 58 Neb. 642, 76 Am. St. Rep. 122. See ante, § 270 et seq.

454 Gardner v. Hope Ins. Co., 9 R. I. 194, 11 Am. Rep. 238; ante, §§ 273-275. But see post, § 631 (f)(2).

455 Mayberry v. Mead, 80 Me. 27; Dewey v. St. Albans Trust Co., 57 Vt. 332; Atlantic De Laine Co. v. Mason, 5 R. I. 463; Regener v. Phillips, 26 Misc. Rep. (N. Y.) 311; Wells v. Green Bay & Mississippi Canal Co., 90 Wis. 442; Price's Appeal, 106 Pa. St. 421; Santa Cruz R. Co. v. Spreckles, 65 Cal. 193; Youngloye v. Steinman, 80 Cal. 375;

Green v. Abietine Medical Co., 96 Cal. 322; Sparks v. Lower Payette Ditch Co., 2 Idaho, 1030; Gary v. York Min. Co., 9 Utah, 464.

Under a statute authorizing a corporation to "assess upon each share of stock such sums of money as the corporation may think proper, not excluding in the whole the amount at which each share was originally limited," the corporation can make such an assessment on stock upon which the par value has already been paid by the subscriber. Price's Appeal, 106 Pa. St. 421. See, also, Santa Cruz R. Co. v. Spreckles, 65 Cal. 193.

Assessments may be levied if an agreement to such effect is in-

Statutes and charters allowing assessments upon full-paid stock are to be strictly construed, and are not to be extended beyond their terms. The assessments can only be levied as authorized.456 The requirements of the statute as to the mode of making the assessments must be complied with.457 If the assessment is required or authorized to be made by consent of a certain proportion of the stockholders, and at a meeting specially called, and with certain notice, it cannot be made without such consent given at such a meeting.458

When a statute authorizes assessments for the purpose of paying debts only, an assessment not only for paying debts, but also for erecting a building and carrying on business, is unauthorized and void.459 And if assessments to a certain amount only are authorized, the limitation cannot be exceeded.460

When the assessment of paid-up stock is authorized by a valid statute, or by the charter or articles of association, for the pur-

Rep. (N. Y.) 306.

456 Dewey v. St. Albans Trust Co., 57 Vt. 332; Mayberry v. Mead, 80 Me. 27; Atlantic De Laine Co. v. Mason, 5 R. I. 463; Lancaster Starch Co. v. Moore, 62 N. H. 671; Louisiana Paper Co. v. Waples, 3 Woods, 34, Fed. Cas. No. 8,540; Great Falls & Conway R. Co. v. Copp, 38 N. H. 124; State v. Mor-ristown Fire Ass'n, 23 N. J. Law, 195, Keener's Cas. 845; Roht v. Sevier Mining & Milling Co., 18 Utah, 290.

457 Mayberry v. Mead, 80 Me. 27; Atlantic De Laine Co. v. Mason, 5 & Milling Co., 18 Utah, 290.

458 Atlantic De Laine Co. v. Mason, of the Milling Co., 18 Utah, 290.

son, 5 R. I. 463; Mayberry v. Mead,

dorsed on the certificates of stock. a corporation was organized de-Weeks v. Silver Islet Consolidated clared that no stockholder should Min. Co., 55 N. Y. Super. Ct. 1. ever be held liable for the con-But the indorsement must be such tracts or faults of such corporation as to show an intention that as- in any further sum than the unsessments may be levied over and paid balance due to the company above the amount of the stock on the shares owned by him, which when it has been full-paid. Sulli- was a mere declaration of the comvan County Club v. Butler, 26 Misc. mon-law rule, and the charter prescribed in what installments forty per cent. of the stock should be paid, and then declared that the balance on each share should not be called for unless with the consent of three-fourths of the stockholders, and then only to increase the business of the corporation, it was held that, after the payment of forty per cent. of his stock, no stockholder was liable for the balance unless called for by a vote of three-fourths of the stockholders. Louisiana Paper Co. v. Waples, 3 Woods, 34, Fed. Cas. No. 8,540.

> 459 Lancaster Starch Co. v. Moore, 62 N. H. 671.

460 Great Falls & Conway R. Co. v. Copp, 38 N. H. 124; State v. Morristown Fire Ass'n, 23 N. J. Where a general law under which Law, 195, 1 Keener's Cas. 845.

pose of paying debts, such an assessment may be levied by a receiver of the corporation.<sup>461</sup> But where the directors of a corporation were authorized by statute to levy an assessment upon paid-up stock for the purpose of repairing the capital stock when impaired by losses or otherwise, it was held that this contemplated assessments to repair the capital with a view to continuing business, and that a receiver of the corporation could not levy assessments for the purpose of paying debts.<sup>462</sup>

A statute authorizing assessments does not authorize unequal assessments. They must be just and equal on all the stockholders.  $^{463}$ 

#### V. AMOUNT OF CAPITAL STOCK, AND INCREASE OR REDUCTION THEREOF.

§ 405. In general.—The amount of the capital stock of a corporation is that fixed by its charter or the general law under which it is formed, or by its articles or certificate of association or incorporation under authority conferred by the charter or general law; and it cannot be changed without legislative authority. A change in the amount of the capital of a corporation does not affect the amount of its capital stock.

A corporation cannot increase its capital stock beyond the amount originally fixed, even with the consent of all the stockholders, unless the power to do so is conferred upon it by the legislature. And when authority is so conferred, it must be exercised subject to the conditions, and in the mode, if any, prescribed by the statute or charter. An attempted increase without any authority is absolutely void; but where an increase is authorized, stockholders may be estopped to set up failure to comply with prescribed conditions or formalities.

When the capital stock of a corporation is increased under legislative authority, existing stockholders have the right, in preference to any other person and as between themselves, to subscribe for or purchase the new stock in proportion to the num-

<sup>461</sup> Regener v. Phillips, 26 Misc.

463 Green v. Abietine Medical Co.,

Rep. (N. Y.) 311.

96 Cal. 322.

<sup>462</sup> Dewey v. St. Albans Trust Co., 57 Vt. 332.

ber of shares of the original stock held by them respectively, unless there is some statutory or charter provision or some agreement to the contrary, or unless they have waived the right. And this privilege may be sold or assigned by them.

A corporation cannot reduce the amount of its capital stock, directly or indirectly, without legislative authority.

When the number of shares into which the capital stock of a corporation is divided and their par value is fixed by the legislature, no change can be made therein without legislative authority. It is otherwise if they are not so fixed, and the change is so made as not to increase or reduce the amount of the capital stock.

## § 406. Amount of original capital stock.

The amount of the capital stock which a corporation is authorized or required to have is fixed by the charter or the general law under which it is formed, or by its articles or certificate of association or incorporation under authority of the charter or general law, and it is well settled that, when the amount thereof is so fixed, it cannot be changed, even with the consent of all the stockholders, directly or indirectly, unless the power to change the same has been expressly conferred by the legislature.464 "The legal capital stock of a corporation," said the New York court of appeals, "is that fixed by its charter, or by authority derived from the legislature. A corporation has no implied authority to increase or diminish its capital stock."465

If the charter of a corporation or the general law does not fix the amount of its capital stock, it must be fixed by the stockholders or directors, and this must be done before a subscriber for shares can be held liable on his subscription.466 In such a case, it may be fixed by the stockholders, or by the directors

<sup>464</sup> Crandall v. Lincoln, 52 Conn. 73, 52 Am. Rep. 560; Salem Mill Tenn. 476, 17 Am. St. Rep. 910. Dam Corporation v. Ropes, 6 Pick. (Mass.) 23, 2 Keener's Cas. 1245; State v. Morristown Fire Ass'n, 23 N. J. Law, 195, 1 Keener's Cas. 845; Sutherland v. Olcott, 95 N. Y. v. Cushing, 45 Me. 524.

<sup>100;</sup> Cartwright v. Dickinson, 88

<sup>465</sup> Sutherland v. Olcott, 95 N. Y. 100.

<sup>466</sup> Somerset & Kennebec R. Co.

under authority from the stockholders, at such amount as they may see fit. 467 A statute authorizing the members of a corporation to determine the amount of the capital stock, and to issue the same to the persons incorporated to the amount of their interest, authorizes the issue of stock to any amount, and to any persons designated by the members.468

As was explained in a former section, the capital stock of a corporation is not the same thing as its capital, the capital stock being the fund contributed by the stockholders for the purposes of the corporation, and the capital being the actual assets of the corporation. The capital may be increased by surplus profits, or diminished by losses, but this does not increase or diminish the amount of the capital stock. "The funds of the company may fluctuate. Its capital stock remains invariable, save by legislative enactment."469

#### § 407. Increase and overissue of stock.

(a) In general.—When the charter of a corporation, or the general law under which it is formed, or its articles of association under authority thereby conferred, fixes the amount of its capital stock, as is invariably the case, the corporation is absolutely without the power to afterwards increase the same. directly or indirectly, even with the consent of all the stockholders, except in so far as the power to do so has been expressly or impliedly conferred upon it by the legislature; and

of shares should be determined from time to time by the directors, and that, as soon as two hundred and fifty shares should be subscribed, the company might construct its road, and after more than Ass'n, 23 N. J. Law, 195, 1 Keener's

467 Somerset & Kennebec R. Co. been subscribed, the directors votv. Cushing, 45 Me. 524; Com. v. ed to close the subscription books, Central Passenger Ry., 52 Pa. St. it was held that the vote was in 506; State v. Bank of Commerce, effect a vote fixing the number of shares to be issued for the time be-Where an act incorporating a ing at the number then subscribed. railroad company provided that its as ascertained by the subscription capital stock should not exceed two books. Lexington & West Camthousand shares, that the number bridge R. Co. v. Chandler, 13 Metc. (Mass.) 311.

> 468 Com. v. Central Passenger Ry. Co., 52 Pa. St. 506.

469 State v. Morristown two hundred and fifty shares had Cas. 845. And see ante, § 375. any overissue of stock is therefore void. No principle in the law of corporation is more surely settled than this.470

To constitute an overissue, within this rule, there must be an issue of stock in excess of the amount authorized. When a corporation which has already issued the full amount of its stock accepts a surrender of, or purchases, or forfeits the shares of one of the stockholders, and afterwards reissues the same. this does not constitute an overissue. 471 Nor is there an overissue where a corporation issues new certificates of stock in lieu of other certificates, properly issued, which have been lost or destroyed.472

(b) Grant of power by the legislature.—Power to increase its capital stock beyond the amount originally fixed, or to increase the same from time to time, may be conferred upon a corporation by its charter or the general law under which it is organized, or by the articles of association under authority of the charter or general law, 473 provided the grant of power does not violate any constitutional provision. 474 The articles of associa-

 $^{470}$  State v. Morristown Fire McCord v. Ohio & Mississippi R. Ass'n, 23 N. J. Law, 195, 1 Keen- Co., 13 Ind. 220; Clark v. Turner, er's Cas. 845; New York & New 73 Ga. 1. Haven R. Co. v. Schuyler, 34 N. Y. So, 1 Keener's Cas. 874, 2 Smith's 54 Mo. App. 41.
Cas. 1109, 2 Cum. Cas. 119; President, etc., of the Mechanics' Bank v. New York & New Haven R. Co., Co., 1 Misc. Rep. (N. Y.) 457, 140
13 N. Y. 599; Sutherland v. Olcott, N. Y. 183. 95 N. Y. 93; People v. Parker Vein Coal Co., 10 How. Pr. (N. Y.) 543; Rep. 203; Laredo Imp. Co. v. Stevenson (C. C. A.) 66 Fed. 633; Anthony v. Household Sewing-Machine Co., 16 R. I. 571; Grangers'
Life & Health Ins. Co. v. Kamper, tional prohibition against an in-73 Ala. 325; Cartwright v. Dickinson, 88 Tenn. 476, 17 Am. St. Rep. except on the assent of the holders 910; Chicago City Ry. Co. v. Allerof a majority of the stock at a ton, 18 Wall. (U. S.) 233, 1 Keener's Cas. 867, 1 Cum. Cas. 752; sixty days' notice, it was held that Kampman v. Tarver, 87 Tex. 491; a statute authorizing an increase

471 Wells v. Thompson Mfg. Co.,

478 Gray v. President, etc., of the Portland Bank, 3 Mass. 364, 3 Am. Coal Co., 10 How. Fr. (N. Y.) 543; Fortland Bank, 3 Mass. 354, 3 Am. Einstein v. Rochester Gas & Electric Co., 77 Hun (N. Y.) 149, 146

N. Y. 46, 1 Keener's Cas. 870; Scovenson (C. C. A.) 66 Fed. 633; vill v. Thayer, 105 U. S. 143, 2 Wellersburg & W. N. Plank Road Keener's Cas. 897; McNulta v. Corn

Belt Bank, 164 III. 427, 56 Am. St. Chamber of Commerce v. Secretary

tion of a corporation, however, cannot give it the power to increase its capital stock, unless such a provision is authorized by the law under which it is organized; and if such a provision is inserted in the articles without authority, it is void.475 There has been a conflict of opinion as to whether the legislature has the power to amend the charter of a corporation by authorizing it to increase its capital stock, and make the amendment binding upon dissenting stockholders when accepted by a majority of the stockholders.476

It has been held that, when the charter of a corporation or the general law gives it the power to fix its capital stock by by-law, it may at any time increase the same by amendment of its by-This, however, is doubtful.478

Whether or not a particular statute confers upon a corporation the power to increase its capital stock, and the extent of the power, depend, of course, upon a construction of the stat-Some of the decisions in which the statutes have been construed are given in the note below and in subsequent notes. 479

on the written assent of the holders of three-fourths of the original stock, being in contravention of the constitution, was void, and that an attempted increase in compliance therewith was therefore void. Ewing v. Oroville Min. Co., 56 Cal. 649.

475 Eastern Plank Road Co. v. Vaughan, 14 N. Y. 546; Grangers' Life & Health Ins. Co. v. Kamper, 73 Ala. 325; Laredo Imp. Co. v. Stevenson (C. C. A.) 66 Fed. 633; Kampman v. Tarver, 87 Tex. 491.

A statute providing that a corporation may provide by its articles of association for an increase of its capital stock authorizes it to amend its articles so as to increase its capital stock, but the same formalities as to filing and publishing the amendment are necessary as are required of the original articles. Palmer v. Bank merce v. Gardner, 109 Mich. 691.

476 See post, chapter xxiv. 477 Peck v. Elliott (C. C. A.) 79

Fed. 10.

478 That there is no such power was held in Ross-Meehan Brake Shoe Foundry Co. v. Southern Malleable Iron Co., 72 Fed. 957.

479 A statute authorizing the formation of corporations for manufacturing and other which authorizes the trustees to purchase property necessary for their business, and issue stock to the amount and value thereof, in payment, does not authorize the issue of stock in addition to their capital stock in payment, but refers only to the capital stock. Schenck v. Andrews, 46 N. Y. 589.

Where a corporation whose stock was divided into preferred and common stock was authorized by statute to increase its capital stock. and nothing was said as to the of Zumbrota, 72 Minn. 266. See, class to which the increased stock also. Detroit Chamber of Com-should belong, it was held that the inference was that it was common The power is generally conferred in express terms, but it may be impliedly conferred. Thus, authority given to a corporation to issue bonds convertible into stock at the option of the holder, necessarily includes the power to issue such an amount of stock as may be necessary to enable the corporation to perform its contract, although the issue may increase its capital stock beyond the amount fixed by its charter. 480

If there is any limitation as to the amount of the increase. the corporation has no more power to exceed the limit than it would have if no power to make any increase at all were given.481 If the charter of a corporation allows it to fix the capital stock within certain limits, it may commence with the minimum amount, and subsequently increase it up to the limit.482

As a rule, the increase must be made in the mode and with the formalities, if any, prescribed by the statute, and all express conditions precedent to the right to make an increase must

St. Rep. 650.

(C. C. A.) 66 Fed. 633.

Under a statute providing that a corporation may increase its capital stock to any amount "not exceeding double the amount of its authorized capital," where a corporation increases its capital stock more than double the amount of original authorized capital stock, the increase is invalid, whether it is attempted to be made at one or more times. Berg v. San Antonio Street Ry. Co., 17 Tex. Civ. App. 291.

Where an act authorized corporations to increase their capital stock to not exceeding double the amount of their authorized capital stock, by a vote of the stockholders, and a later amendatory act Dec. 156.

stock. Jones v. Concord & Monprovided that any corporation treal R., 67 N. H. 119, 234, 68 Am. might amend its charter subject to the constitution and laws of the 480 Belmont v. Erie Ry. Co., 52 state and the provisions of the act, Barb. (N. Y.) 637; Ramsey v. it was held that the limitation in Erie Ry. Co., 38 How. Pr. (N. Y.) 193. See post, § 422. increase the capital stock was not 481 Kampman v. Tarver, 87 Tex. 491; Laredo Imp. Co. v. Stevenson that a corporation could not, by that a corporation could not, by changing their articles of incorporation, increase their capital stock beyond double the amount originally fixed. Laredo Imp. Co. v. Stevenson (C. C. A.) 66 Fed. 633; Kampman v. Tarver, 87 Tex. 491.

Where a railroad company was authorized to increase its capital stock for the extension of its road, and by a later statute the capital stock required was reduced onehalf, it was held that the later statute was enabling, not restrictive, and that an increase in excess of the amount thereby required was valid. Agricultural Branch R. Co. v. Winchester, 13 Allen (Mass.) 29.

482 Gray v. President, etc., of the Portland Bank, 3 Mass. 364, 3 Am.

be performed or fulfilled: 483 but mere informalities and irregularities, as we shall hereafter see, will not necessarily render the increase void.484

- (c) Necessity for increase.—When the legislature authorizes a corporation to increase its capital stock to a certain amount for a certain purpose, the courts will not, in an action by a stockholder to enjoin an issue of increased stock, inquire into the necessity for the increase.485
- (d) Ratification of unauthorized increase.—The legislature may ratify and render valid an increase of its stock by a corporation, which was unauthorized when made, or which was made without compliance with statutory requirements, although it cannot thereby impair vested rights. 486

An agreement to issue stock when there is no power to issue the same, if absolute, and not conditional upon the power being subsequently conferred, is illegal and void, and is not rendered valid and binding by a subsequent grant of power to issue the stock.487

(e) Restriction or impairment of power-Exaction of fee or bonus.—In granting to a corporation the power to increase its capital stock, the legislature may, subject to constitutional limitations, impose any conditions it may see fit. It may exact a bonus or require payment of a fee to the state.488 But if the

483 Page v. Austin, 10 Can. Sup. coln v. New Orleans Express Co., 45 La. Ann. 729; Winters v. Arminfra, this section, (h).

484 Nelson v. Hubbard, 96 Ala. 238. See infra, this section, (h),

485 Jones v. Concord & Montreal R. I. 571. R., 67 N. H. 119, 234, 68 Am. St. Rep. 650.

486 Turnbull v. Pomeroy Salt Co., 24 Wkly. Law Bul. (Ohio) 133.

487 Where a corporation agreed to Ct. 132; McCord v. Ohio & Misrepay a loan in preferred stock to sissippi R. Co., 13 Ind. 220; Linbe subsequently issued, and it was ann. 729; Winters v. Arm-no power to issue such stock, it strong, 37 Fed. 508; Nichols v. Stewas held that the lender could phens, 32 Mo. App. 330; Jones v. maintain an action against the corcord & Montreal R., 67 N. H. poration for the return of the ret afterwards ascertained that it had fore the trial authorizing issue of such stock, as the contract was illegal and a nullity. Anthony v. Household Sewing Machine Co., 16

488 The Illinois act of 1895, requiring all corporations "at present organized," that may increase their capital stock, to pay a fee, charter of a corporation gives it the unconditional right to increase its capital stock, and the right to alter, amend, or repeal the charter is not reserved, the constitutional prohibition against laws impairing the obligation of contracts prevents the state from afterwards taking away or impairing such right, by exacting a bonus or otherwise.<sup>489</sup>

(f) How and by whom the increase must be made or authorized.

—Since legislative authority is necessary to enable a corporation to increase its capital stock, the increase can only be accomplished legally in the mode and subject to the limitations, if any, prescribed by the legislature in authorizing the increase. 490 If no mode of issuing the increased stock is prescribed by the legislature, it may be fixed by the stockholders. 491

An increase of the capital stock of a corporation beyond the

was held to include corporations subsequently organized, since the object of the act was to raise revenue, and another statute of that state provided that statutes shall be construed so as to carry out the intent with which they were enacted, and that words in the present tense include the future. People v. Hinrichsen, 161 III. 223.

489 Com. v. Erie & Western Transportation Co., 107 Pa. St. 112. See

ante, § 270 et seq.

490 McNulta v. Corn Belt Bank, 164 Ill. 427, 56 Am. St. Rep. 203; Winters v. Armstrong, 37 Fed. 508; State v. McGrath, 86 Mo. 239; Nichols v. Stephens, 32 Mo. App. 330; Schierenberg v. Stephens, 32 Mo. App. 314; Ohio Ins. Co. v. Nun-nemacher, 15 Ind. 294; McCord v. Ohio & Mississippi R. Co., 13 Ind. 220; Union Ry. Co. v. Sneed, 99 Tenn. 1; Lincoln v. New Orleans Express Co., 45 La. Ann. 729; Jones v. Concord & Montreal R., 67 N. H. 119, 234, 68 Am. St. Rep. 650; Laredo Imp. Co. v. Stevenson (C. C. A.) 66 Fed. 633; Kampman v. Tarver, 87 Tex. 491; Page v. Austin, 10 Can. Sup. Ct. 132; Shepp v. Norristown Passenger Ry. Co., 13 Pa. Co. Ct. R. 254.

But informalities or irregularities will not necessarily render the increase void. See infra, this section, (h), (j).

If a corporation is authorized to increase its capital stock to an amount not exceeding double its originally authorized stock, and it increases it to a larger amount, the entire increase is void. Kampman v. Tarver, 87 Tex. 491; Laredo Imp. Co. v. Stevenson (C. C. A.) 66 Fed. 633.

Where an amendment of the articles of incorporation is necessary to authorize an increase of capital stock, and a statute declares that an amendment of articles of incorporation shall be inoperative until a certificate of the same is left for record in a certain office, an increase before such a certificate is left for record is invalid. Wood v. Union Gospel Church Bldg. Ass'n, 63 Wis. 9.

In the absence of evidence to the contrary, performance of conditions, as the payment of a tax, for example, will be presumed. Peck v. Elliott (C. C. A.) 79 Fed, 10.

<sup>491</sup> See Stephenson v. Vokes, 27 Ont. (Can.) 691.

limit fixed by its charter or articles of association is so organic and fundamental a change that a general power to make the increase granted by the charter must be exercised by the stockholders, or with their consent. It cannot be exercised by the directors without the consent of the stockholders, unless it is expressly so provided.492 Such power is not conferred upon the directors by provisions in the charter of a corporation that its capital stock may be increased from time to time, at the pleasure of the corporation, and that "all the corporate powers of the said corporation shall be vested in and exercised by a board of directors and such officers and agents as said board shall appoint," for such general power to perform corporate acts refers to the ordinary business transactions of the corporation, and does not extend to a reconstruction of the body itself, or to an enlargement of its capital stock. 493 Authority to increase the capital stock may be expressly conferred upon the directors of a corporation by its charter. 494 Or, in the absence of charter or statutory provisions to the contrary, if the power exists in the corporation, it may be conferred upon the directors by the stockholders by a formal vote at a corporate. meeting.495 Or if the directors have exercised the power, and made the increase, without previous authority from the stockholders, the stockholders may render the increase valid by rati-

492 Chicago City Ry. Co. v. Allerton, 18 Wall. (U. S.) 233, 1 Keener's Cas. 867, 1 Cum. Cas. 752; Eidman v. Bowman, 58 Ill. 444, 11 Am. Rep. 90; McNulta v. Corn Belt Bank, 164 Ill. 427, 56 Am. St. Rep. 203; Humboldt Driving Park Ass'n v. Stevens, 34 Neb. 528, 33 Am. St. Rep. 654; Finley Shoe & Leather Co. v. Kurtz, 34 Mich. 89; Percy v. Millandon, 3 La. 568; Newport Cotton Mill Co. v. Mims, 103 Tenn. 465; post, chapter xxiv.

A resolution passed by the board of directors of a corporation cannot fix, in advance, the time for increasing its capital stock, without reference to the action of the stockholders. McNulta v. Corn Belt

492 Chicago City Ry. Co. v. Aller-Bank, 164 Ill. 427, 56 Am. St. Rep. n. 18 Wall (U.S.) 233 1 Keep. 203

<sup>493</sup> Chicago City Ry. Co. v. Allerton, 18 Wall. (U. S.) 233, 1 Keener's Cas. 867, 1 Cum. Cas. 752.

494 See Sutherland v. Olcott, 95
 N. Y. 93; Payson v. Stoever, 2 Dill.
 427, Fed. Cas. No. 10,863; Payson v. Withers, 5 Biss. 269, Fed. Cas. No. 10,864.

That an amendment of the charter of a corporation so as to authorize the directors, instead of the stockholders, to increase the capital stock, does not release dissenting stockholders, see post, § 482.

reference to the action of the stockholders. McNulta v. Corn Belt and cases in the note following.

fication, and if they acquiesce in such action on the part of the directors, it is equivalent to a ratification. 496

A vote of the stockholders to increase the capital stock may be reconsidered and revoked at any time before the additional stock is actually issued, or at least subscribed for, in pursuance thereof, for until then the stock is not increased.497

National banks have no authority to increase their capital stock except as provided by Rev. St. U. S. § 5142, and the act of congress of May 6, 1886; and where an increase is attempted to be made without obtaining the consent of the holders of twothirds of the stock, the payment in full of the amount of the increase, and the approval and certificate of the comptroller of the currency, as required by those statutes, the proceedings are invalid, and preliminary subscriptions to such increase cannot be enforced, in the absence of elements of estoppel. Such a subscription is impliedly conditioned on the subscription of the whole amount of the proposed increase, and on compliance by the corporation with all the requirements of the statutes necessary to make the increased stock valid; and in case of noncompliance with such requirements, there is a failure of consideration.498

(g) Effect of unauthorized increase or agreement therefor.-If a corporation undertakes to increase its capital stock without authority, and issues certificates for the additional stock, or if its officers or agents fraudulently issue certificates in excess of the amount authorized, the corporation, as we shall hereafter see, may be liable in damages to bona fide purchasers of the certificates. 499 The increase and the certificates, however, are void, because of the fact that it is beyond the powers of the corporation to create and issue the additional stock, and the

<sup>496</sup> Sewell's Case, 3 Ch. App. 131; Eidman v. Bowman, 58 Ill. 444, 11 Am. Rep. 90; Payson v. Stoever, 2 Dill. 427, Fed. Cas. No. 10,863.

Conn. 141.

<sup>498</sup> Winters v. Armstrong, 37 Fed.

<sup>499</sup> New York & New Haven R. Co. v. Schuyler, 34 N. Y. 30, 1 Keener's Cas. 874, 2 Smith's Cas. 497 Terry v. Eagle Lock Co., 47 1109, 2 Cum. Cas. 119. See post, § 428 et sea.

holders of the certificates, therefore, whether they be the original holders or their bona fide transferees, do not become stockholders, 500 except, under some circumstances, as to creditors. 501 An unauthorized increase of capital stock is none the less void because made by unanimous agreement among the stockholders, and under an honest misapprehension as to their powers.<sup>502</sup>

It follows that, when an increase of the capital stock of a corporation is unauthorized, the holders of certificates for the new stock cannot vote the same at corporate meetings. If they undertake to do so, the votes are void. 503 And subscriptions for the new stock are absolutely void, both as between the corporation and the subscribers, 504 and, subject to some limitation, even as against creditors.<sup>505</sup> An agreement to issue stock when there is no power to issue the same is illegal and void.506

500 New York & New Haven R. Co. v. Schuyler, 34 N. Y. 30, 1 Keener's Cas. 874, 2 Smith's Cas. 1109, 2 Cum. Cas. 119; Seovill v. Thayer, 105 U. S. 143, 2 Keener's Cas. 897; Page v. Austin, 10 Can. Sup. Ct. 132.

If a statute authorizing an increase of capital stock requires that the full amount of the original capital stock shall be first paid in, an attempted increase before fulfillment of this condition is void. Page v. Austin, 10 Can. Sup. Ct.

The fact that a person has paid money to a corporation for increased shares of capital stock does not make him a stockholder, where the increase was unauthorized. Schierenberg v. Stephens, 32 Mo.

App. 314.

As to the effect of a statutory or constitutional provision that no corporation shall issue stock except for money, labor done, or money or property actually received, and that a fictitious increase of stock shall be void, see Fitzpatrick v. Dispatch Publishing Co., 83 Ala. 604; Grant v. East & West R. Co. of Alabama, 13 U.S. App. 1, 54 Fed. 569: Stein v. Howard, 65 Cal. 616, 2 Keener's Cas. 963; Michigan ing Machine Co., 16 R. I. 571.

Southern & Northern Indiana R. Co. v. Auditor General, 9 Mich. 448; Knowlton v. Congress & Empire Spring Co., 14 Blatchf. 364. Fed. Cas. No. 7,903; Spring Co. v. Knowlton, 103 U. S. 49. And see ante, § 391 et seq.

501 See infra, this section, (j).

502 People v. Parker Vein Coal Co., 10 How. Pr. (N. Y.) 543.

503 Humboldt Driving Park Ass'n v. Stevens, 34 Neb. 528, 33 Am. St. Rep. 654.

Total Cartwright v. Dickinson, 88 Tenn. 476, 17 Am. St. Rep. 910; Kampman v. Tarver, 87 Tex. 491; Laredo Imp. Co. v. Stevenson (C. C. A.) 66 Fed. 633; Ross-Meehan Brake Shoe Foundry Co. v. Southern Malleable Iron Co., 72 Fed. 957.

See, also, Union R. Co. v. Sneed, 99 Tenn. 1; Clark v. Turner, 73 Ga. 1; Level Land Co. v. Hayward, 95 Wis. 109; Mackley's Case, 1 Ch. Div. 247; Lathrop v. Kneeland, 46 Barb. (N. Y.) 432; Burrows v. Smith, 10 N. Y. 550; Scovill v. Thayer, 105 U. S. 143, 2 Keener's Cas. 897, 2 Smith's Cas. 818,

505 Infra, this section, (j).

506 Anthony v. Household Sew-

Certificates of stock issued by the officers or agents of a corporation in excess of its authorized capital stock will be canceled at the suit of the corporation, or at the suit of a stockholder on behalf of himself and the other stockholders, if the corporation refuses to sue,507 unless the remedy is barred by laches or elements of estoppel. 508

An unauthorized increase of stock does not affect the validity of the original stock. 509

(h) Effect of informalities and irregularities.—As was stated in a preceding paragraph, since legislative authority is necessary to enable a corporation to increase its capital stock, the increase, when authorized, cannot be legally accomplished except in the mode and subject to the limitations, if any, prescribed by the legislature.<sup>510</sup> To be legal as against the state, the increase must be voted and made in the mode and with the formalities prescribed by the legislature in authorizing it. Thus, if the statute authorizing an increase of stock requires notice of the intended increase to be published, and this formality is omitted, the secretary of state may properly refuse to file the certificate which the statute requires to be filed.<sup>511</sup>

Informalities and irregularities may also render an increase of stock invalid as against original stockholders who are not estopped by participation or acquiescence. 512 And if the rights of creditors are not involved, 513 informalities or irregularities, if they consist in the omission of essential steps prescribed by the statute authorizing the increase, will entitle subscribers for

<sup>507</sup> New York & New Haven R. it was held that his right to have Co. v. Schuyler, 34 N. Y. 30, 1 the excessive stock canceled was Keener's Cas. 874, 2 Smith's Cas. lost by laches. Jutte v. Hutchin-1109, 2 Cum. Cas. 119; post, § 536 son, 189 Pa. St. 218.

<sup>508</sup> See infra, this section, (h). Where the holder of a portion of the preferred stock of a bridge company failed to complain of an overissue of stock, greatly in excess of the amount required to build the bridge, for nearly six following. years after the issue of the stock,

<sup>509</sup> Byers v. Rollins, 13 Colo. 22.

<sup>510</sup> Supra, this section, (f). 511 State v. McGrath, 86 Mo. 239.

<sup>512</sup> See Jones v. Concord & Montreal R., 67 N. H. 119, 234, 68 Am. St. Rep. 650, and cases in the notes

<sup>513</sup> See infra, this section, (j).

the increased stock to avoid their subscriptions and recover what they have paid thereon, unless they are estopped. 514

Failure to comply with provisions in the statute which are intended merely for the benefit and protection of the stockholders may be waived by them.<sup>515</sup> And, generally, both original

514 Brown v. Tillinghast, 84 Fed. 71; Tillinghast v. Bailey, 86 Fed. 46: Lincoln v. New Orleans Express Co., 45 La. Ann. 729; Union Ry. Co. v. Sneed, 99 Tenn. 1; Page v. Austin, 10 Can. Sup. Ct. 132.

In an action on a subscription for stock, where the amount of stock was fixed by the charter of the corporation, with a proviso that additional stock might be issued when directed by the president and directors, it was held that the fact that the whole amount of the original stock had been issued, and that the issue of additional stock had not been directed by the president and directors, was a good defense. McCord v. Ohio & Mississippi R. Co., 13 Ind. 220.

The increase must be authorized by the stockholders as required by the statute, or it will be invalid. Nichols v. Stephens, 32 Mo. App. 330; Winters v. Armstrong, 37 Fed.

Where a statute provided that the capital stock of a corporation could be increased only upon public notice for thirty days of a meeting of stockholders, a stockholders' meeting held in accordance with the notice, a vote on the proposed increase, a certificate of proceedings duly signed and verified, and a filing of the certificate in the office of the secretary of state, and declared that, when the certificate should be so filed, the capital stock should be increased as therein set forth, it was held that increased stock could have no validity until full compliance with the provisions tion, were intended for the benefit of the statute, and, therefore, that of the stockholders, and might be a purchaser of the increased stock waived, and that insufficiency of a could rescind and recover the price notice thereunder is waived where paid. Lincoln v. New Orleans Ex- the stockholders disregard it. Nelpress Co., 45 La. Ann. 729.

In the absence of any evidence that due and sufficient notice was not given to all the stockholders of a meeting to increase the capital stock of a corporation, as required by statute, the book of minutes of the meeting, and the certificate, showing that more than two-thirds of the stockholders appeared in person or by proxy, and voted for the increase, was held sufficient to establish regularity of the meeting as against a subscriber for the increased stock. Cuykendall v. Douglas, 19 Hun (N. Y.) 577.

The Connecticut statute requiring a corporation, on increasing its capital stock, to file a certificate of the increase with the secretary of state and town clerk, is intended primarily for the benefit of the public, and its failure to file the same does not render a subscription for increased stock invalid as between the corporation and the subscriber. Barrows v. Natchaug Silk Co., 72 Conn. 658.

515 In Alabama it was held that a constitutional provision that the stock of corporations shall not be increased without the consent of the persons holding the larger amount in value of the stock, first obtained at a meeting held after thirty days' notice, and a statutory provision that, before holding such meeting, notice shall be given for four consecutive weeks in the newspaper published nearest to the place of business of the corporason v. Hubbard, 96 Ala. 238.

stockholders and subscribers for the increased stock are estopped to complain of irregularities or informalities in voting or making the increase, both as against creditors, and as against the corporation and other stockholders or subscribers, if they participated in the proceedings or subscribed for the increased stock with actual or constructive knowledge of the facts, or if they have been guilty of laches, or have acquiesced. 516

In any case, a substantial compliance with the provisions of the statute in voting or making an increase of stock is all that is required. 517 Mere technical objections cannot be set up by a subscriber for the additional stock, to escape liability on his subscription.518

bia Nat. Bank of Tacoma v. Mathews (C. C. A.) 85 Fed. 934; Western Nat. Bank v. Armstrong, 152 U. S. 346; Kansas City Hotel Co. v. Harris, 51 Mo. 464; Kansas City Hotel Co. v. Hunt, 57 Mo. 126; Hoeft v. Kock, 123 Mich. 171.

A stockholder who takes part in a stockholders' meeting at which an increase of stock is voted, either personally or by proxy, cannot afterwards question the validity of the increase on the ground that the meeting was not properly called. Columbia Nat. Bank of Tacoma v. Mathews (C. C. A.) 85 Fed. 934, reversing Matthews v. Columbia Nat. Bank, 79 Fed. 558.

A person who purchases a certificate of increased stock which is not under the seal of the corporation and signed by the president, as required by the statute authorizing the increase, is chargeable with notice of the irregularity, and cannot complain. Byers v. Rollins, 13 Colo. 22.

Stockholders voting an increase of the capital stock, without specifying the time of issuance, waive 57 Mo. 126.

516 Bailey v. Champlain Mining irregularity on the part of the di-& Prospecting Co., 77 Wis. 453; rectors in issuing the same in vari-Southern Plank-Road Co. v. Hixon, ous amounts from time to time 5 Ind. 165; Poole v. West Point during a period of six years, where Butter & Cheese Ass'n, 30 Fed. 513; they accept dividends and parti-Bard v. Banigan, 39 Fed. 13; Banicipate in stockholders' meetings gan v. Bard, 134 U. S. 291; Colum-during such time, without making any objection. Barrows v. Natchaug Silk Co., 72 Conn. 658.

As to when a subscriber is estopped as against creditors of the corporation, see infra, this section.

517 Where a statute required a certificate of a meeting of stockholders for the purpose of increasing the capital stock of a corporation to be "acknowledged" by the chairman, it was held sufficient where a certificate recited that it was "subscribed and sworn to" before a justice of the peace, by the chairman, instead of being "acknowledged." Cuykendall v. Douglas. 19 Hun (N. Y.) 577.

Under a statute providing that, in proceedings to increase the capital stock of a corporation, a certificate shall be filed showing "the amount of capital actually paid in," it was held that a certificate that the whole of the capital stock "has been sold, and all but \$-- paid in," was sufficient. Moosbrugger v. Walsh. 89 Hun (N. Y.) 564.

518 Kansas City Hotel Co.v. Hunt,

When a national bank increases its capital stock, as authorized by the national bank act, the certificate of the comptroller of the currency is conclusive as to the regularity of the proceedings, and a subscriber for the increased stock cannot avoid his subscription and recover what he has paid, merely on the ground of irregularities.519

(i) Subscriptions for new stock.—When an increase of stock is authorized, subscriptions for the new stock are, with a few exceptions, subject to the same rules of law as subscriptions for original stock. Thus, the same principles apply to the formation of the contract as apply to the formation of a contract for original stock after organization of the corporation. 520 subscriptions for new stock, like subscriptions for original stock, may be rescinded, subject to the same qualifications, for false and fraudulent representations. 521 But it cannot be avoided for defects and irregularities in making the increase if the subscriber knew of such defects and irregularities at the time he subscribed, or if he has paid upon his subscription, or otherwise recognized it as binding, since acquiring such knowledge. 522

There are some differences, however, between subscriptions for original stock and subscriptions for new stock on an increase of the capital stock after the formation of the corporation. In the absence of provision to the contrary, a subscriber for original stock in a corporation becomes a stockholder as soon as his subscription is accepted and becomes a binding contract, whether he has paid the amount of the subscription or not. 523 But when a corporation increases its capital stock after its organization, subscribers for the additional shares do not become stockholders with respect to such shares, or acquire any title to the stock, until they have paid for it.524

<sup>519</sup> Columbia Nat. Bank of Tacoma v. Mathews (C. C. A.) 85 Fed. firmed in Newton Nat. Bank v. 934, reversing Matthews v. Columbia Nat. Bank, 79 Fed. 558; Tillinghast v. Bailey, 86 Fed. 46; Lat
522 Kansas City Hotel Co. v. imer v. Bard, 76 Fed. 536.

<sup>520</sup> Post, § 437 et seq.

<sup>521</sup> Newbegin v. Newton Nat.

<sup>522</sup> Kansas City Hotel Co. v. Hunt, 57 Mo. 126.

<sup>523</sup> Post, § 508 et seq.

<sup>524</sup> Baltimore City Passenger Ry.

A subscription for original stock is upon the implied condition that the full amount of the required capital stock shall be subscribed before there shall be any liability on the subscription, unless there is some provision or stipulation to the contrary. <sup>525</sup> But, by the weight of authority, in the absence of an express provision or stipulation, liability upon a subscription for new stock, when the capital stock of a corporation is increased, is not conditional upon the taking of all the new shares. <sup>526</sup>

If a person subscribes for increased stock before the increase is made, and makes a payment on his subscription, and the contemplated increase is not made, he may recover back what he has paid, although the corporation has become insolvent.<sup>527</sup>

Some questions relating to subscriptions for increased stock have been considered in preceding paragraphs. We have seen that subscriptions are absolutely void if the increase was entirely unauthorized by the legislature, <sup>528</sup> and that they may be void because of failure to comply with the provisions of the

te in voting or making the increase.<sup>529</sup> Estoppel as against creditors of the corporation is considered in the paragraph following.

(j) Estoppel as against creditors.—If a corporation increases its capital stock when it has no power to do so under any circumstances, persons subsequently dealing with it are chargeable with notice of its want of power, and they cannot, as creditors of the corporation, contend that the holders of the unauthorized stock are estopped to deny its validity for the purpose of escaping liability as stockholders for the debts of the corpo-

Co. v. Hambleton, 77 Md. 341, 2 Keener's Cas. 1033; St. Paul, Stillwater & T. F. R. Co. v. Robbins, 23 Minn. 439.

525 Post, § 503 et seq.

526 Avegno v. Citizens' Bank, 40
La. Ann. 799; Clarke v. Thómas, 34
Ohio St. 46. See post, § 505.

It may be otherwise by express

provision. Brown v. Tillinghast, 84 Fed. 71.

527 McFarlin v. First Nat. Bank of Kansas City (C. C. A.) 68 Fed. 868; Winters v. Armstrong, 37 Fed. 508. And see American Tube Works v. Boston Machine Co., 139 Mass. 5; Reed v. Boston Machine Co., 141 Mass. 454.

528 Supra, this section, (g).

529 Supra, this section, (h).

ration.<sup>530</sup> It is otherwise, however, where a corporation is authorized to increase its capital stock under certain circumstances, and exceeds its powers, or if there are mere irregularities or informalities in voting or making the increase. In such a case, the holders of the new stock will be estopped to deny its validity as against persons who have become creditors of the corporation in reliance upon its validity.<sup>531</sup> Subscribers for

Turner, 73 Ga. 1.
This is true, even though the

Kampman v. Tarver, 87 Tex. 491.

man v. Upton, 96 U. S. 328; Hand- U. S. 417). ley v. Stutz, 139 U. S. 417, affirm— Where, in amending articles of ing Stutz v. Handley, 41 Fed. 531; incorporation with a view to in-Sayles v. Brown, 40 Fed. 8.

required by statute; it was held same. Fithian v. Weidenborner, 72 that the defect only affected the Minn. 331. See, also, Palmer v. position of the company and the Bank of Zumbrota, 72 Minn. 266, shareholder inter se; and where where it was held that there is no

530 Scovill v. Thayer, 105 U. S. it was held that the shareholder 143, 2 Keener's Cas. 897, 2 Smith's was precluded from objecting to Cas. 818; Kampman v. Tarver; 87 the validity of the increase as a Tex. 491; Ross-Meehan Brake Shoe ground for removing him from the Foundry Co. v. Southern Malleable list of contributories. In re Mil-Iron Co., 72 Fed. 957; Clark v. Ier's Dale & Ashwood Dale Lime Co., 31 Ch. Div. 211.

A subscriber for increased stock holder of such stock may have act- in a corporation cannot escape liaed as a stockholder. Ross-Meehan bility as against creditors on the Brake Shoe Foundry Co. v. South- ground that notice of the increase ern Malleable Iron Co., 72 Fed. 957. was not published as required by Where a corporation increased the statute under which it was its capital stock \$1,100,000, when it made (Handley v. Stutz, 139 U. S. was given the power to increase it 417, 41 Fed. 531); or on the ground \$100,000 only, it was held that the that there was no proper notice or entire increase was void, and that call of the meeting at which the subscribers thereto were not liable increase was voted (Stutz v. Handto creditors of the corporatiom. ley, 41 Fed. 531, 139 U.S. 417. Contra, In re Wheeler, 2 Abb. Pr. 531 In re Miller's Dale & Ashwood [N. S.; N. Y.] 361); or that the Dale Lime Co., 31 Ch. Div. 211; meeting was held in another state Chubb v. Upton, 95 U. S. 665; Pull- (Stutz v. Handley, 41 Fed. 531, 139

Peck v. Elliott (C. C. A.) 79 Fed. creasing the capital stock of a cor-10; Upton v. Jackson, 1 Flip. 413, poration, statutory requirements as 10; Upton v. Jackson, 1 Filp. 413, poration, statutory requirements as Fed. Cas. No. 16,802; Veeder v. to the execution, filing, and publi-Mudgett, 95 N. Y. 295; Fithian v. cation of the amendment are not Weidenborner, 72 Minn. 331; Latimer v. Bard, 76 Fed. 536; Clark is voted for by the stockholders, v. Turner, 73 Ga. 1; Hoeft v. Kock, the increased stock issued, and 123 Mich. 171; Palmer v. Bank of held by the new stockholders until Zumbrota, 72 Minn. 266. Compare the corporation becomes insolvent. and an action is commenced for the Where a director of a company appointment of a receiver, the holdtook shares of increased stock is- ers of the new stock are estopped sued under a resolution passed and to deny the validity of the increase confirmed at meetings the interval as against creditors who have bebetween which was less than that come such on the faith of the the company went into liquidation, estoppel as against persons who

increased stock are not estopped to set up that the increase was irregular and invalid, as against creditors who were managers and stockholders of the corporation, and participated in the increase 532

One who subscribes and pays for a proposed increase of stock in a corporation, as a national bank, for example, is not subject to the statutory liability to creditors, as a "shareholder," where the increase is in fact never made, and the officers of the corporation, instead of the increased stock subscribed and paid for, transfer to him old stock of the bank, without his knowledge or consent.533

crease.

In Page v. Austin, 10 Can. Sup. Ct. 132, it was held that there was that the shares held by them were shares of increased stock, and that cause the whole of the original capital stock had not been paid in at the time of the increase, as was required by a statute.

A holder of certificates of stock in a national bank cannot escape liability as a stockholder to creditors under Rev. St. U. S. § 5151, on the ground that the shares of stock which the certificates represent are part of an increase which was made without compliance with the conditions of the act of May 1, 1886 (24 St. at Large, p. 18, c. 73), which prohibits increase of capital stock until the whole amount of such increase is paid in, and the comptroller of the currency has certified to that fact. And this is true, even though he may have been induced to take the stock by fraud of the officers of the bank and of the comptroller. Scott v. Deweese, 181 U. S. 202, 21 Sup. Ct. 585.

A subscriber for a proposed increase of stock in a national bank, 842.

became creditors before the in- who has made payments on his subscription, believing that statutory requirements would be complied with so as to make a valno estoppel, even in favor of cred- id increase, is entitled to have the itors, where they sought to enforce amount of such payments allowed a statutory liability against alleged as a claim against the assets of the stockholders, of the latter to show bank in the hands of a receiver. Winters v. Armstrong, 37 Fed. 508.

In an action by the receiver of a the increase was unauthorized be- national bank to enforce subscriptions to a proposed increase of its capital stock, an allegation that the bank, subsequent to the defendants' subscriptions, and with knowledge, represented to the public, by means of circulars, letter heads, etc., that its capital stock had been increased, and that the defendants allowed their names to remain upon the list of those subscribing for and entitled to such increased stock, but without alleging that the public gave credit to the bank on the faith that the defendants were part owners of such increase of stock, or that the defendants allowed themselves to be held out as actual 'stockholders, does not show that they are estopped to plead the failure of the bank to comply with the statutory requirements in making the increase. Winters v. Armstrong, 37 Fed. 508.

532 Sayles v. Brown, 40 Fed. 8. 533 Stephens v. Follett, 43 Fed.

#### § 408. Rights and remedies of existing stockholders with respect to new stock.

As a general rule, when a corporation increases its capital stock under authority conferred by the legislature, stockholders at the time of the increase have the right, in preference to any other person, and as between themselves, to subscribe for or purchase the new stock in proportion to the number of shares of the original stock held by them respectively; and a majority of the stockholders or the officers of the corporation cannot lawfully deprive any stockholder of this right. 534 applies, of course, to such persons only as are stockholders, and entitled to be recognized as such by the corporation, at the time the new stock is created.535

Ill. 444, 11 Am. Rep. 90; Humboldt Driving Park Ass'n v. Stevens, 34 Neb. 528, 33 Am. St. Rep. 654; State v. Smith, 48 Vt. 286; Baltimore City Passenger Ry. Co. v. Hambleton, 77 Md. 341, 2 Keener's Cas. 1033; Gibbons v. Mahon, 4 Mackey, D. C. 136, 136 U. S. 549; Knapp v. Publishers: George Knapp & Co., 127 Mo. 53; Reading Trust Co. v. Reading Iron Works, 137 Pa. St. 282; Wells v. Green Bay & Mississippi Canal Co., 90 Wis. 442; Way v. American Grease Co. (N. J. Eq.) 47 Atl. 44.

A vote at a stockholders' meeting directing the new stock to be sold, without giving a stockholder an opportunity to subscribe therefor. is void as to him, unless he consents. Jones v. Morrison, 31 Minn.

It was contended, in an early South Carolina case, that a corporation had no power to give its shareholders the preference in disposing of a new issue of stock; but it was held that it could do so if not prohibited by its charter or by statute. State v. Bank of Charleston, Dud. (S. C.) 187.

534 Gray v. President, etc., of the ital stock does not give the pro-Portland Bank, 3 Mass. 364, 3 Am. posed increase any existence, so Dec. 156; Jones v. Morrison, 31 as to give stockholders any vested Minn. 140; Eidman v. Bowman, 58 right thereto, and if the vote is rescinded, no right is acquired. Terry v. Eagle Lock Co., 47 Conn.

Placing new stock "to the credit of" a stockholder is sufficient to show an intent to pass the title to him, as against the company. Knapp v. Publishers: George Knapp & Co., 127 Mo. 53.

As to the stockholders' right to any premium on a sale of new stock by the corporation, see infra, this section.

535 Miller v. Illinois Central R. Co., 24 Barb. (N. Y.) 312.

Additional stock issued by a corporation follows the title recognized by it, and does not pass to a buyer of stock under an executory contract, without an express stipulation to that effect. Currie v. White, 1 Sweeney (N. Y.) 166.

Persons holding corporate bonds or notes convertible into stock at their option are not entitled to the preference, for until the bonds or notes are converted into stock, they are not stockholders. Pratt v. American Bell Tel. Co., 141 Mass. 225, 55 Am. Rep. 465.

Holders of preferred stock are A mere vote to increase the cap- entitled to the privilege. Jones v.

This rule may be rendered inapplicable by the peculiar provisions of the charter of the corporation, under which the increase is made, 536 or by special agreements, assignments, or other special circumstances.<sup>537</sup> And a stockholder may waive the privilege, or forfeit the same by laches or acquiescence. 538

This doctrine clearly applies when a corporation increases its capital stock by making a stock dividend. It cannot discriminate between stockholders, but each stockholder is enti-

Concord & Montreal R., 67 N. H. 119, 234, 68 Am. St. Rep. 650.

As between the pledgor pledgee of stock, the former is entitled to the privilege. Miller v. Illinois Central R. Co., 24 Barb. (N. Y.) 312.

536 In an Indiana case it was held that under the charter of an insurance company, which provided that the directors should have the power to increase the capital stock to a certain limit on such terms and conditions, and in such manner, as to them should seem best, it was held that existing stockholders had no exclusive right to take the new stock in proportion to the original stock held by them. Ohio Ins. Co. v. Nunnemacher, 15 Ind. 294.

Where a mining and manufacturing corporation was organized for the purchase of property with stock, under the New Jersey law, it was held that such provision became a part of the contract between the stockholders and the corporation; and where new stock was issued for the purchase of mines, which would become a part of the common property, from which all of the stockholders would receive the same benefit, original holders could not insist that the new stock be issued to them in the proportion their holdings bore to the whole amount of stock before the increase. Meredith v. New Jersey Zinc & Iron Co., 56 N. J. Eq. 454, affirming 55 N. J. Eq. 211.

146 N. Y. 46, 1 Keener's Cas. 870.

538 Hart v. St. Charles Street R. Co., 30 La, Ann. 758.

Where the charter of a corporation provided for sixty days' notice of authorization of any increase of the capital stock, within which any stockholder might have the privilege of taking additional shares, it was held that any stockholder not applying and tendering payment within such time waived or forfeited his privilege. Hart v. St. Charles Street R. Co., 30 La. Ann. 758.

In Wilson v. Bank of Montgomery County, 29 Pa. St. 537, it was held that a stockholder could not recover from the corporation the value of his proportionate share of an increase of stock for which the corporation refused to permit him to subscribe, where he made no offer to subscribe for the stock until six months after its issuance.

The right to take new shares may be lost by failure to comply with the terms upon which they are offered. Sewall v. Eastern R. Co., 9 Cush. (Mass.) 5.

Where, under a resolution of the stockholders of a corporation, each stockholder is given the right to purchase increased stock at par, in proportion to his holdings, a stockholder who is unwilling or unable to take the stock on the terms offered cannot complain that the stockholders taking the stock gained an advantage over him, as his 537 See Einstein v. Rochester Gas right to take the stock may be sold. & Electric Co., 77 Hun (N. Y.) 149, Jones v. Concord & Montreal R., 67 N. H. 119, 234, 68 Am. St. Rep. 650.

tled to receive new shares in proportion to the stock held by him at the time the dividend is made. 539

The doctrine, as we have seen, does not apply to shares of its original stock undisposed of by the corporation when it commences business, nor to shares of original stock reacquired by a corporation by forfeiture of the same for nonpayment of assessments, or by purchase, or by compromise with the holders. Such shares constitute a part of its assets, and may be sold by it either to stockholders or to strangers, as it may deem best. 540

Remedies.—If the right to a preference in subscribing for new stock is denied to any stockholder by the corporation, he may maintain a special action of assumpsit against it to recover damages, for the case is within the established doctrine that most of the duties imposed upon a corporation by law raise an implied promise which, when broken, will sustain an action of assump-The measure of damages in such an action has been held to be the excess of the market value above the par value of the number of shares he was entitled to at the time he demanded his certificates and they were refused, with interest on such excess up to the time when judgment is rendered.542

If a corporation denies to a stockholder the right to subscribe for or purchase his proportion of the new shares, there is undoubtedly a breach of trust, as well as a breach of implied contract, and if the corporation has the shares, there is no reason why the stockholder may not, instead of suing for damages,

see post. § 523(f).

540 Ante. § 388.

v. Newark Plank-Road Co., 31 N. J. W. 325. Law, 277, 2 Cum. Cas. 201; Reese

539 See the cases above cited; and damages for depriving him of his right to subscribe for new shares, he must show that he demanded shares and offered to subscribe and 541 Gray v. President, etc., of the pay for them in the regular man-Portland Bank, 3 Mass. 364, 3 Am. ner. Bonnet v. First Nat. Bank of Dec. 156. And see Jackson's Adm'rs Eagle Pass (Tex. Civ. App.) 60 S.

The statute of limitations does v. Bank of Montgomery County, 31 not begin to run until the right Pa. St. 78, 72 Am. Dec. 726; Read- is denied. Wells v. Green Bay & ing Trust Co. v. Reading Iron Mississippi Canal Co., 90 Wis. 442. Works, 137 Pa. St. 282. In an action by a stockholder Portland Bank, 3 Mass. 364, 3 Am. against the corporation to recover Dec. 156. sue in equity for an injunction and to enforce his right to subscribe for or purchase the stock.<sup>543</sup>

Sale or assignment of privilege.—A stockholder's right to a preference in subscribing for or purchasing the new stock, when the capital stock of a corporation is increased, may be sold or assigned by him.<sup>544</sup> When shares of original stock are sold by the holder after an increase of the capital stock has been voted, the purchaser acquires, as an incident to the stock, the same right to a preference in subscribing for or purchasing the new stock as was possessed by the transferrer.<sup>545</sup>

Charging stockholders a bonus.—Where a statute provides that, where a corporation increases its capital stock, or the par value of its stock, the new shares shall be allotted *pro rata* to the stockholders according to their interests, stockholders cannot be charged a *bonus* on increased stock to which they are given a right to subscribe. But a *bonus* demanded by a corporation of its stockholders for the privilege of subscribing to an issue of new stock, and paid by them under protest, cannot be

543 See Dousman v. Wisconsin & L. S. Mining & Smelting Co., 40 Wis. 418; Wells v. Green Bay & Mississippi Canal Co., 90 Wis. 442. Compare, however, Meredith v. New Jersey Zinc & Iron Co., 55 N. J. Eq. 211, 56 N. J. Eq. 454.

Where the directors of a corporation, upon an increase of the capital stock, disregard the right of stockholders to subscribe for the new stock, and, for the purpose of securing themselves in office and in the control of the corporation, issue the stock to their friends for less than its par value, defrauded stockholders may sue in equity to set the issue aside and enforce their rights, and to enjoin the holders of the stock from voting at corporate elections, and the corporation from receiving their votes. Way v. American Grease Co. (N. J. Eq.) 47 Atl. 44.

544 Jones v. Concord & Montreal R., 67 N. H. 119, 234, 68 Am. St. Rep. 650; Atkins v. Albree, 12 Allen (Mass.) 359. As to failure of a purchaser of the privilege to comply with the terms on which the stock is offered, see Sewall v. Eastern R. Co., 9 Cush. (Mass.) 5.

<sup>545</sup> Baltimore City Passenger Ry. Co. v. Hambleton, 77 Md. 341, 2 Keener's Cas. 1033.

A stockholder who transfers his shares is not entitled to subscribe for a subsequent increase of capital stock, but the transferee is entitled to do so, under a statute providing that stockholders at the time of an increase of stock shall be entitled to a pro rata share thereof. Real Estate Trust Co. v. Bird, 90 Md. 229.

The transferee's rights are not affected by an agreement between the transferrer and the other stockholders, of which he has no notice, waiving the right to subscribe for a pro rata share of the new stock. Id.

546 Cunningham's Appeal, 108 Pa. St. 546.

recovered back, in the absence of duress. And it has been held that a denial of a stockholder's right to the new shares without payment of the bonus does not constitute duress, since, after a tender, he may sue and recover the market value of the stock, and with this sum buy other shares.547

Rights as between life beneficiary of shares and remainderman.— When shares of stock are transferred or bequeathed in trust to pay the income to a person for life (or for a term of years), and the corporation increases its capital stock, the privilege of subscribing for the new shares is appurtenant to the old stock, and does not belong to the life beneficiary.<sup>548</sup> If the trustee, being unable to subscribe for the new shares, sells his right to subscribe, the money received is to be treated as the new shares would be treated, and not as a profit on the original shares, and therefore the life beneficiary is only entitled to the income therefrom. 549

The right to dividends, including stock dividends, as between life beneficiary and remainderman, is elsewhere considered. 550

# § 409. Sale of new stock by corporation.

Of course, the increased stock may be sold by the corporation, like its original unissued stock, if the stockholders consent or waive their privilege. 551 And a sale of the same is sometimes provided for by statute.<sup>552</sup> Thus it is sometimes provided

Co. of North America, 136 Pa. St. capital, and not income, and did 62, 658.

548 Hite v. Hite, 93 Ky. 257, 40 Am. St. Rep. 189; Atkins v. Albree, 12 Allen (Mass.) 359. See, also, Spooner v. Phillips, 62 Conn. 62; Gibbons v. Mahon, 4 Mackey (D. C.) 130, 54 Am. Rep. 262; Brown's Petition, 14 R. I. 371, 51 Am. Rep. 397.

Where trustees exchanged stock, on the consolidation of the corporation with another, for stock in the consolidated company, and received additional certificates to reper. 15 Ind. 294; Meredith v. New resent the difference in value of Jersey Zinc & Iron Co., 56 N. J.

547 De La Cuesta v. Insurance held that the additional stock was not go to the life beneficiary. Clarkson v. Clarkson, 18 Barb. (N. Y.) 646.

> 549 Atkins v. Albree, 12 Allen (Mass.) 359; Moss' Appeal, 83 Pa. St. 264, 24 Am. Rep. 164; Biddle's Appeal, 99 Pa. St. 278. Compare, however, Wiltbank's Appeal, 64 Pa. St. 256.

<sup>550</sup> See post, § 526.

<sup>551</sup> Ante. § 408.

<sup>552</sup> Ohio Ins. Co. v. Nunnemachthe old stock over the new, it was Eq. 454, affirming 55 N. J. Eq. 211;

that when a corporation increases its capital stock, and the new stock is worth more than par, it shall be sold at public auction to the highest bidders,553 or that so much of the new stock as is not subscribed for or purchased by the stockholders in pursuance of their privilege shall be so sold. The statutory provisions in this respect must be followed. 554 It has been said, independently of any statutory provision, that new stock not taken by the stockholders should be sold at public auction,555 but it would seem that this is a matter within the discretion of the corporation unless it is controlled by some express statutory provision. To hold otherwise is judicial legislation.

It has been held that, when new stock in a corporation is created and sold at a premium, the premium is the property of the stockholders, 556 but this is not the law unless it is so agreed or provided by statute.557

## Liabilities arising out of increase of stock.

The liability of subscribers for increased stock has been considered in a former section, 558 and the liability of a corporation

168 Mass. 345.

553 See Attorney General v. Boston & Maine R. R., 109 Mass, 99.

554 Under a statute providing that, when a corporation increases its capital stock, the shares not taken by the stockholders shall be sold by the directors "at public auction," a private sale, so long as it is executory, is void, and a purchaser of shares at a private sale cannot compel the issue of certificates therefor. Smith v. Franklin Park Land & Imp. Co., 168 Mass.

Under a statute providing that, when a corporation shall increase its capital stock, each stockholder may take his proportion, and the shares not so taken "may be sold or issued in such manner as its stockholders may by vote direct," etc., the stockholders must direct

Attorney General v. Boston & the manner of sale, and cannot del-Maine R. R., 109 Mass. 99; Smith egate this power to an officer. v. Franklin Park Land & Imp. Co., Smith v. Franklin Park Land & Imp. Co., 168 Mass. 345.

> 555 In re Wheeler, 2 Abb. Pr. (N. S.; N. Y.) 361.

> 556 State v. Franklin Bank of Columbus, 10 Ohio, 91, 97.

> 557 Under a statute providing that, whenever a corporation shall increase its capital stock, the shares not taken by the stockholders may be sold or issued in such manner as the stockholders shall by vote direct, but no shares shall be sold for less than their par value, a stockholder who has not taken his proportion of new shares of stock so issued has no right to a premium obtained on a sale thereof pursuant to a vote of the stockholders, unless the vote so provides. Mason v. Davol Mills, 132 Mass. 76.

558 Ante, § 407(i).

in damages arising out of an overissue of stock will be considered in subsequent sections. <sup>559</sup> Certain other questions will be treated here.

By statute in some jurisdictions,—New York, for example, the stockholders of a corporation are subjected to individual liability for the debts of the corporation until the full amount of the capital stock is paid in, and a certificate stating such fact recorded, and the statute applies to an increase of capital stock as well as to original stock. As to the increase, however, it only applies to the holders of that stock. When the original capital stock of a corporation is fully paid in, and a certificate filed stating the amount thereof and the fact of payment, as required by a statute imposing individual liability upon stockholders for debts of the corporation until this is done, the individual liability of the holders of the original stock is then at an end, and cannot be revived by a subsequent increase of the capital stock. The holders of the original stock of a corporation, therefore, are not liable thereon because of a failure to pay in the increased capital stock. The liability rests solely on the holders of the increased stock.560

Even when a corporation is authorized to increase its capital stock, it may do so under such circumstances as to perpetrate a fraud upon the public, and in such a case, not only the corporation, but its original stockholders and officers as well, may be liable therefor. If the directors and a majority of the stockholders of a corporation, knowing it to be insolvent, enter into a scheme to fraudulently increase its capital stock, representing and pretending that it is not indebted, and that the increase is for the purpose of enabling it to enlarge its business, and that it has been and is prosperous and successful, and thereby induce persons to purchase and pay for the new stock, the corporation and the guilty directors and stockholders are liable for the damages sustained by the purchasers by reason

<sup>559</sup> Post, § 428 et seq. 295; Griffeth v. Green, 129 N. Y. 560 Veeder v. Mudgett, 95 N. Y. 517.

of the conspiracy and fraud. The corporation is liable because the increase is a corporate act, and the directors and stockholders are liable because of their participation.<sup>561</sup>

#### § 411. Reduction of capital stock.

(a) In general.—As a general rule, when the amount of the capital stock of a corporation is fixed by its charter or articles of association, or by the general law, it has no more power, in the absence of authority from the legislature, to reduce the same, either directly or indirectly, than it has to increase the same. Any change, to be valid, must be expressly authorized. 562 In the absence of legislative authority, therefore, a corporation cannot reduce its capital stock from the amount fixed by its charter or articles to the amount actually paid in. 563 A corporation cannot reduce its capital stock by purchasing its own shares for cancellation or retirement. 564 If it undertakes to do so, and pays for the shares out of the assets of the company, creditors of the company, on its becoming insolvent, may hold the stockholders liable in equity to the extent of the assets so received by them. 565

It has been held that a corporation cannot purchase its own shares for the purpose of holding them, on the ground that the purchase by a corporation of its own shares in effect reduces its capital stock to that extent until the shares are reissued. 566

561 Dorsey Machine Co. v. McCaffrey, 139 Ind. 545, 47 Am. St. Rep.

562 Droitwich Patent Salt Co. v. Curzon, L. R. 3 Exch. 35, 1 Keener's Cas. 861; Holmes v. Newcastleupon-Tyne Abattoir Co., 45 L. J. Ch. 383; Seignouret v. Home Ins. Co., 24 Fed. 332; Crandall v. Lincoln, 52 Conn. 73, 52 Am. Rep. 560; Cartwright v. Dickinson, 88 Tenn. 476, 17 Am. St. Rep. 910; Ferris v. Ludlow, 7 Ind. 517; Coquard v. St. Louis Cotton Compress Co. (Mo.) 7 S. W. 176; In re State Ins. Co., 14 Fed. 28. See, also, In re Ebbw Vale Steel, Iron & Coal Co., 4 Ch. weah Canal & Irrigation Co. (Cal.) Div. 827; Bannatyne v. Direct 44 Pac. 662.

Spanish Telegraph Co., 34 Ch. Div. 287; In re Direct Spanish Telegraph Co., 34 Ch. Div. 307; Salem Mill Dam Corp. v. Ropes, 6 Pick. (Mass.) 23, 2 Keener's Cas. 1245.

563 Droitwich Patent Salt Co. v. Curzon, L. R. 3 Exch. 35, 1 Keener's Cas. 861.

564 Cartwright v. Dickinson, 88 Tenn. 476, 17 Am. St. Rep. 910; Crandall v. Lincoln, 52 Conn. 73, 52 Am. Rep. 560.

565 Crandall v. Lincoln, 52 Conn. 73, 52 Am. Rep. 560.

566 Tulare Irrigation Dist. v. Ka-

Strictly speaking, however, this is not in any sense a reduction of the capital stock. 567 The power of a corporation to purchase and hold its own shares is elsewhere considered.<sup>568</sup>

If the charter of a corporation does not fix the amount of the capital stock, and it is fixed by the stockholders or directors, and if the whole amount fixed is not taken, they may afterwards reduce it to the amount taken.<sup>569</sup>

As we shall see in another section, when a stockholder cannot pay for his shares, the corporation, if the transaction is in good faith, may accept a surrender of the shares, and release him from further liability.<sup>570</sup> This, however, is not a reduction of the capital stock, for the shares may be reissued to subscribers or purchasers.<sup>571</sup>

(b) Reduction under legislative authority.—It is within the power of the legislature to authorize a corporation to reduce the amount of its capital stock by a provision to that effect in its charter or the general law in force at the time it is organized, or by an amendment after its creation or organization. But a grant to a corporation of authority to increase its capital. stock does not include the power to reduce the same.<sup>572</sup>

When a corporation is authorized to reduce its capital stock. it may do so by purchasing its shares and canceling or retiring the same. 578 Or it may accept a surrender of shares, and give the holders in exchange therefor a proportionate amount of its assets, provided no rights of creditors are involved.<sup>574</sup> Or it may do so by canceling shares which have not yet been issued. 575

A statute providing that a corporation, "at any meeting called for the purpose, may increase or reduce its capital stock and

<sup>567</sup> See infra, this section, (d).

<sup>568</sup> Ante, § 199 et seq.

<sup>569</sup> Somerset & Kennebec R. Co. v. Cushing, 45 Me. 524.

<sup>570</sup> Post, § 476.

<sup>571</sup> See infra, this section, (d).

<sup>572</sup> Droitwich Patent Salt Co. v. ber Co., 97 Wis. 585, Curzon, L. R. 3 Exch. 35, 1 Keen- 575 In re Gatling G er's Cas. 861: Seignouret v. Home 628.

Ins. Co., 24 Fed. 332; Sutherland v. Olcott, 95 N. Y. 93.

<sup>573</sup> British & American Trustee & Finance Corp. v. Couper, [1894] App. Cas. 399; In re Gatling Gun, 43 Ch. Div. 628; Shoemaker v. Washburn Lumber Co., 97 Wis. 585.

<sup>574</sup> Shoemaker v. Washburn Lum-

<sup>575</sup> In re Gatling Gun. 43 Ch. Div.

the number of shares therein," does not authorize a corporation to reduce its capital stock by purchasing the shares of a particular stockholder, unless all consent. In order that such a reduction may operate justly to all the stockholders, each stockholder should be allowed to surrender such proportion of his stock as the amount of the proposed reduction bears to the whole amount of the capital stock.<sup>576</sup>

A corporation cannot, by a by-law or otherwise, force a stock-holder to sell his shares for the purpose of canceling and retiring them, and thereby reducing the capital stock.<sup>577</sup>

In order that there may be a reduction of the capital stock of a corporation, action upon the part of the corporation to that end is necessary, and, as a rule, the special requirements of the statute, if any, must be substantially complied with.<sup>578</sup> Although a reduction of its capital stock by a corporation may be irregularly made, however, as where the proceedings for the reduction are begun before filing of its certificate of organization, and completed after it is filed, the reduction is not necessarily void, and persons who afterwards become creditors of the corporation, not being injured, cannot complain of the irregularity, and hold the released shareholders liable.<sup>579</sup>

A resolution of a corporation to reduce its capital stock is sometimes required to be approved and confirmed by some court; and when the power thus conferred upon a court is a discretionary power, a resolution to reduce capital stock will not be confirmed where it will work injustice between different classes of stockholders, as between common and preferred stockholders.

576 Currier v. Lebanon Slate Co., 56 N. H. 262, 1 Keener's Cas. 685.

Nor can the stock be reduced, without the consent of all the stockholders, by allowing a particular stockholder to withdraw his subscription. Niagara Shoe Co. v. Tobey, 71 Ill. App. 250.

577 Bergman v. St. Paul Mutual

577 Bergman v. St. Paul Mutual Building Ass'n No. 1, 29 Minn. 275. 578 Moses v. Ocoee Bank, 1 Lea (Tenn.) 398; Ferris v. Ludlow, 7

Ind. 517; Gade v. Forest Glen Brick & Tile Co., 165 Ill. 367. An informality in the vote taken

An informality in the vote taken to reduce the capital stock of a corporation, as authorized by a statute, does not affect the existence of the corporation. Brown v. Wyandotte & S. E. R. Co., 68 Ark. 134.

579 Gade v. Forest Glen Brick & Tile Co., 165 Ill. 367.

580 See, as to confirmation by the

(c) Effect of reduction.—When a corporation reduces its capital stock under legislative authority, the shares retired or reduced no longer exist for any purpose. Thus, neither the remaining shareholders nor the former holders of the retired shares are subject to the statutory liability to creditors attaching to such shares.<sup>581</sup> When a corporation reduces its capital stock under proper authority by purchasing some of its shares, and paying therefor by a proportionate amount of its assets, a person who afterwards becomes a creditor of the corporation cannot complain.582

The capital stock of a corporation, however, cannot be reduced to the prejudice of existing creditors. Thus, if a corporation undertakes to retire shares and release the subscribers from liability thereon for the amount unpaid on their subscriptions, the release is ineffectual as against existing creditors.<sup>583</sup> Nor can a corporation, as against existing creditors, purchase shares for the purpose of reducing its capital stock, and pay the holders therefor from the assets of the corporation.<sup>584</sup> it attempts to do so, creditors may maintain a suit in equity to enjoin the transaction, even though their claims are not vet due. $^{585}$ 

Where all the shares of stock of a corporation are of the same class, and the capital stock is reduced because of losses, the loss on the reduction must be borne by all the stockholders alike in proportion to their shares. But when there are different classes of shares, the loss on such reduction must fall

Div. 287; In re Hyderabad (Dec- 87; Palfrey v. Paulding, 7 La. Ann. can) Co., 75 L. T. (N. S.) 23. 363. S81 Moon Bros. Carriage Co. v. 583 Dane v. Young, 61 Me. 160; In

Co., 13 Tex. Civ. App. 103.

It is otherwise if the purchase is not authorized. Currier v. Leba- Co., L. R. 10 Eq. 384. non Slate Co., 56 N. H. 262. 582 Shoemaker v. Washburn Lum- Co., L. R. 10 Eq. 384.

court under the English statute, In ber Co., 97 Wis. 585. And see Coopre Direct Spanish Telegraph Co., er v. Frederick, 9 Ala. 738; Hep-34 Ch. Div. 307; Bannatyne v. Diburn v. Commissioners of Exrect Spanish Telegraph Co., 34 Ch. change & Banking Co., 4 La. Ann.

Waxahachie Grain & Implement re State Ins. Co., 14 Fed. 28; Bedford R. Co. v. Bowser, 48 Pa. St. 29. 584 In re Telegraph Construction

585 In re Telegraph Construction

upon those who would have to bear it if there was a winding up.586

When the amount of the capital stock of a corporation is lawfully reduced under legislative authority, the corporation is not required to keep the excess of its actual capital over the amount of its nominal capital as reduced, nor has it any right to do so; but the stockholders have the right to have it divided among them, as in the case of a dividend, in proportion to their shares. 587 In making such distribution, however, regard must be had to the present value of the property, and the company, instead of distributing money or property equal in value to the excess of the original nominal capital and the reduced nominal capital, must retain property equal in present value to the reduced nominal capital, after deducting its debts. In other words, the surplus, if any, which a corporation may pay to its stockholders on reducing its capital stock, must inc.ery case 'e ascertained, and depends upon the result of an examination into its affairs, and not upon the difference between the original amount of capital stock and the reduced amount. 588 Whenever, by sales of property, or by means of earnings, or otherwise, the corporation comes into the possession of funds which are in excess of the amount of its reduced. capital stock, it can distribute that amount among the stockholders.589

Where the stockholders in a national bank, the capital of which had become impaired by reason of past-due and suspended claims, to avoid a threatened assessment by the comptroller of the currency to make good the deficiency, lawfully reduced the capital stock in an amount equal thereto, and some of the suspended claims were afterwards realized upon and

<sup>586</sup> In re London & New York
Inv. Corp., [1895] 2 Ch. Div. 860.

587 Seeley v. New York National v. New York National Exchange Exchange Bank, 8 Daly (N. Y.)

588 Strong v. Brooklyn Cross-Town R. Co., 93 N. Y. 426; Seeley v. New York National Exchange Exchange Bank, 8 Daly (N. Y.)

588 Strong v. Brooklyn Cross-Town R. Co., 93 N. Y. 426; Seeley v. New York National Exchange Exchange Bank, 8 Daly (N. Y.)

588 Strong v. Brooklyn Cross-Town R. Co., 93 N. Y. 426; Seeley v. New York National Exchange 400, 78 N. Y. 608; Strong v. Brook-lyn Cross-Town R. Co., 93 N. Y. 426.

<sup>589</sup> See the cases above cited.

carried into the account as assets of the bank, it was held that a stockholder could not compel the bank to distribute a share of the money so realized in proportion to the amount of stock surrendered by him.590

(d) Effect of purchase of shares by corporation.—When a corporation purchases shares of its own stock, as it may lawfully do under some circumstances, and as it may also do unlawfully,591 the shares are not thereby merged or extinguished, unless such is the intention. If it does not intend to retire the shares, they merely remain in suspension, as it were, and may be at any time reissued. This is true, whether the purchase of the shares was intra vires or ultra vires. 592

# Increase or reduction in number of shares and their par

Although there is no reduction or increase of a corporation's capital stock where the number of shares into which it is divided is changed, and a corresponding change is made in the par value of the shares,—as where the number of shares is doubled, and the par value of each share reduced one-half,—yet, if the charter of a corporation fixes the number and par value of its shares, such a change cannot be made without express authority from the legislature. 593 There is nothing to prevent such

Jeffersonville, 112 Ind. 354, 131 Ind. ams, 49 La. Ann. 1350.

<sup>591</sup> Ante, § 199 et seq.

592 City Bank of Columbus v. Corp., 2 Ch. App. 714; Tschumi v. Bruce, 17 N. Y. 507; Hartridge v. Hills, 6 Kan. App. 549; Salem Mill Rockwell, R. M. Charlt. (Ga.) 260; Western Imp. Co. v. Des Moines 23, 2 Keener's Cas. 1245.

Nat. Bank, 103 Iowa, 455; Bank of A. corporation has no power to San Luis Obispo v. Wickersham, 99 change the number or the par val-Cal. 655; Chillicothe Branch of ue of the shares of its capital State Bank of Ohio v. Fox, 3 stock as fixed by its charter. Blatchf. 431, Fed. Cas. No. 2,683; Shares of stock purporting to be Com. v. Boston & Albany R. Co., 142 Mass. 146; American Railwav-Frog Co. v. Haven, 101 Mass. 398. that they shall be of the par value 3 Am. Rep. 377; State v. Smith. 48 of one dollar, are void. Tschumi Vt. 266; Williams v. Savage Mfg. v. Hills, 6 Kan. App. 549.

590 McCann v. First Nat. Bank of Co., 3 Md. Ch. 418; Belknap v. Ad-

<sup>593</sup> Droitwich Patent Salt Co. v. Curzon, L. R. 3 Exch. 35, 1 Keener's Cas. 861; In re Financial

San Luis Obispo v. Wickersham, 99 change the number or the par val-

a change, however, if the number and par value of the shares have not been so fixed, but have been left to be fixed by the corporation.<sup>594</sup>

An increase or reduction in the number of shares without any change in the par value, or an increase or reduction in the par value without any change in the number, is an increase or reduction of the capital stock, as the case may be, and is invalid unless expressly authorized.<sup>595</sup>

- VI. PREFERRED OR GUARANTIED STOCK; INTEREST BEARING STOCK; SPECIAL STOCK.
- § 413. In general.—"Preferred stock," as distinguished from "common stock," is stock which entitles the holders to receive dividends out of surplus profits available for the payment of dividends, to the extent agreed upon, before any dividends are payable to the holders of common stock, and also, when it is so stipulated, but not otherwise, to a preference over the holders of common stock on a distribution of capital.

Guarantied stock is preferred stock upon which a certain dividend is guarantied, so that, if there are not sufficient profits to pay the same in one year, the dividend for that year must be paid in subsequent years, if there are profits available for the purpose, before payment of any dividends on common stock.

Interest bearing stock is like ordinary preferred stock, except that, instead of dividends, a certain interest is payable out of profits.

If the issue of preferred stock is authorized by the charter or articles of association of a corporation, or by a general law in force at the time the stockholders become such, the corporation may issue preferred stock by a vote of a majority of the stockholders, against the dissent of the minority; but if the issue of such stock is not so provided for, it cannot be issued without the consent of all the stockholders, unless under an amendatory stat-

<sup>594</sup> Ambergate, Nottingham & B. re European Central Ry. Co., L. R. & E. J. Ry. Co. v. Mitchell, 4 Exch. 8 Eq. 438. 540; In re County Palatine Loan

<sup>&</sup>amp; Discount Co., 9 Ch. App. 54; 595 See Droitwich Patent Salt Co. Somerset & Kennebec R. Co. v. v. Curzon, L. R. 3 Exch. 35, 1 Cushing, 45 Me. 524. Compare In Keener's Cas. 861.

ute passed by the legislature under a reservation of the power to alter or amend the charter. Express authority from the legislature is not necessary to render valid an issue of preferred stock if all the stockholders consent.

Preferred stock makes the holders thereof stockholders, and not creditors; and, except-as to the preference in the payment of dividends, gives them the same rights, and no greater, and subjects them to the same liabilities, as the holders of common stock, except in so far as they may be given other rights, or relieved from liabilities, by the charter or by statute, or by the valid terms of their contract. As against creditors, they have no greater rights than common stockholders, and the corporation cannot give them greater rights in the assets of the corporation as against creditors. unless by virtue of an express statutory provision.

### § 414. Preferred or guarantied stock—In general.

The ordinary stock-of a corporation, or "common stock," as it is called, gives no stockholder any greater rights than any other stockholder. There is no difference between the shares, but all the stockholders stand upon an equal footing, and each is entitled to share in the profits of the corporation, whenever they are distributed in the way of dividends, in proportion to the number of shares held by him. 596 Preferred stockholders, however, stand on a different footing. As the term implies, preferred stock gives the holder a preference over the holders of common stock with respect to the payment of dividends. Holders of preferred stock are entitled to receive dividends on their shares, to the extent agreed upon, before any dividends at all are paid to the holders of the common stock.597

The expression "guarantied stock" is used interchangeably with "preferred stock." Such stock is preferred stock,—stock upon which the payment of a certain dividend at specified

Cas. 347; Chaffee v. Rutland R. Co., 55 Vt. 110; Belfast & Moosehead Co., 4 Kay & J. 1; Kent v. Quicksilver Min. Co., 78 N. Y. 159, 2 Keener's Cas. 936; Taft v. Hartford, Providence & F. R. Co., 8 R. Am. St. Rep. 650; Totten v. Tison, I. 310, 5 Am. Rep. 575, 1 Smith's 54 Ga. 139. Cas. 347; Chaffee v. Rutland R. Co.,

<sup>596</sup> See post, § 523(f).

periods is guarantied before payment of any dividend to other stockholders. But the guaranty is not absolute, so as to create the relation of debtor and creditor between the corporation and the holders of such stock, irrespective of whether there are profits. It is a guaranty of the specified dividends out of profits available for the payment of dividends. 598 Guarantied stock, however, differs from other preferred stock in that the dividend thereon is guarantied, so that, if there are no profits out of which the dividend can be paid at any time when it is payable according to the terms of the guaranty, the dividend is not necessarily lost, but the holders of the stock will be entitled to payment of all arrears before any payments can be made to the holders of common stock. 599 Such a contract, it was said in an English case, is "a charge on all accruing profits, at the stipulated rate, before anything is divided among the ordinary shareholders. This is, substantially, interest chargeable exclusively on profits."600

Dividends on preferred or guarantied stock are called "preferred or guarantied dividends."601

# § 415. Power to issue preferred or guarantied stock.

(a) In general.—If the charter of a corporation or the general law in force at the time of its creation expressly authorizes it to issue preferred or guarantied stock, as is often the case, there can be no question as to its power in this respect, so long as it keeps within the power so conferred, and the power

Co., 4 Kay & J. 1, 1 De Gex & J. Ry. Co., 84 N. Y. 157, 2 Keener's 606, 3 Jur. (N. S.) 1133; Taft v. Cas. 1368; post, § 529(d).

Hartford, Providence & F. R. Co., 8 R. I. 310, 5 Am. Rep. 575, 1 Smith's Cas. 347; Lockhart v. Van (N. S.) 1133 Alstyne, 31 Mich. 76, 18 Am. Rep. 156, 2 Keener's Cas. 1354; Miller v. Mass. 388; post, § 529.

598 Henry v. Great Northern Ry. Lake Shore & Michigan Southern

600 Henry v. Great Northern Ry. (N. S.) 1133.

601 Henry v. Great Northern Ry. Ratterman, 47 Ohio St. 141; Field Co., 4 Kay & J. 1, 1 De Gex & J. v. Lamson & Goodnow Mfg. Co., 162 606, 3 Jur. (N. S.) 1133; Miller v. Ratterman, 47 Ohio St. 141; Taft v. 599 Henry v. Great Northern Ry. Hartford, Providence & F. R. Co., 8 Co., 4 Kay & J. 1, 1 De Gex & J. 606, R. I. 310, 5 Am. Rep. 575, 1 Smith's 3 Jur. (N. S.) 1133; Boardman v. Cas. 347. may be exercised by a vote of a majority of the stockholders, against the dissent of the minority.602 And it is well settled that, even when no such power is expressly conferred upon a corporation at the time of its creation, it is implied, in the absence of prohibition or restriction, subject to the qualification that it must be exercised for a legitimate corporate purpose, and that the contract rights of shareholders cannot be impaired.603 Such power clearly exists, notwithstanding the dissent of a minority of the stockholders, if it is authorized Lthe articles of association of the corporation, or '7 by-laws adopted by the corporation prior to the issuance of common stock, for in such a case no rights of stockholders are impaired. And the power may be exercised after the issuance of common stock, at any time, if all the stockholders consert 604 know nothing in the constitution or the law," said to mage Folger in a leading New York case, "that inhibits a corporation from beginning its corporate action by classifying the shares in its capital stock, with peculiar privileges to one share over another, and thus offering its stock to the public for subscriptions thereto. No rights are got until a subscription is made. Each subscriber would know for what class of stock he put down his name, and what right he got when he thus became a stock-There need be no deception or mistake; there would be no trenching upon rights previously acquired; no contract, express or implied, would be broken or impaired."605

Havemayer v. Bordeaux Co., 8 Nat. Keener's Cas. 921. Corp. Rep. 127 (III. Cir. Ct. 605 Kent v. Quicksilver Min. Co., 1894); Lockhart v. Van Alstyne, 78 N. Y. 159, 2 Keener's Cas. 936.

602 See Kent v. Quicksilver Min. 31 Mich. 76, 18 Am. Rep. 156, 2 Co., 78 N. Y. 159, 2 Keener's Cas. Keener's Cas. 1354; Higgins v. Lan-936; Belfast & Moosehead Lake R. singh, 154 Ill. 301; Hazlehurst v. Co. v. City of Belfast, 77 Me. 445. Co. v. City of Belfast, 77 Me. 445. Savannah, Griffin & N. A. R. Co., 43 603 Kent v. Quicksilver Min. Co., Ga. 13; In re South Durham Brew-78 N. Y. 159, 2 Keener's Cas. 936, ery Co., 31 Ch. Div. 261; In re and cases in the notes following. Bridgewater Navigation Co., 39 Ch. and Cases in the notes following.

604 Kent v. Quicksilver Min. Co.,
78 N. Y. 159, 2 Keener's Cas. 936; Co., L. R. 19 Eq. 358; Andrews v.
Hamlin v. Continental Trust Co. of
City of New York, 47 U. S. App.
422, 78 Fed. 664; Banigan v. Bard,
234 U. S. 291, affirming 39 Fed. 13;
514, 521, 4 De Gex, J. & S. 672, 2

Preferred stock, however, cannot be issued, against the dissent of a holder of common stock, if his contract with the corporation will be thereby broken or impaired. Therefore, if a corporation, when it issues common stock, is not expressly authorized to issue preferred stock either by its charter or by the general law, and if there is no provision for such stock in its articles of association, it cannot afterwards issue the same without the unanimous consent of the holders of the common stock. 606

The legislature may confer upon a corporation the power to issue preferred stock by an amendment of its charter after the issue of common stock, if all the stockholders consent, but whether such an amendment can be accepted by a majority of the stockholders, so as to bind a dissenting minority, is not so The weight of authority, however, is to the effect that the legislature may make such an amendment and authorize its acceptance by a majority of the stockholders, if there is no express provision in the charter against it, as the amendment does not change the character of objects of the corporation, but is in furtherance of the enterprise for which it was created. 607

(b) By-laws authorizing preferred stock.—By-laws of a corporation may properly provide for the issue of preferred stock, if adopted by unanimous consent of the stockholders, or if adopted by a majority, provided, provision for the issue of such stock is made in the charter of the corporation, or the general law in force at the time of its creation, or in its articles of

78 N. Y. 159, 2 Keener's Cas. 936; Knoxville, Cumberland Gap & L. R. Co. v. City of Knoxville, 98 Tenn. 1; Moss v. Syers, 32 L. J. Ch. 711; Ernst v. Elmira Municipal Imp. Co., 24 Misc. Rep. (N. Y.) 583.

In a New York case, where a corporation and all its registered stockholders signed an agreement to pay debts, forty per cent. of the bell v. American Zylonite Co., 122 stock was surrendered and can-celled, and in place thereof new 822.

stock, entitled to a first lien upon 607 Post, chapter xxiv.

606 Kent v. Quicksilver Min. Co., the net profits for dividends of ten per cent. was issued and sold, it was held that such action was not within the powers of the corporation or stockholders, and therefore was not binding upon one who held stock under an unregistered assignment in blank as security for a debt, and that, upon default and a sale thereof, the purchaser was entitled to a new certificate giving whereby, in order to raise money the same rights as the old. Camp-

association.<sup>608</sup> But, since "the power to make by-laws is to make such as are not inconsistent with the constitution and the law; and the power to alter has the same limit, so that no alteration could be made which would infringe a right already given and secured by the contract of the corporation,"<sup>609</sup> the power to make and alter by-laws, whether expressly granted or implied, cannot give a corporation the power to provide by a by-law for the issue of preferred stock, against the dissent of a holder of common stock, where there is no provision therefor in the charter or general law or articles of association.<sup>610</sup>

An expressly granted or implied power to borrow money.— An expressly granted or implied power to borrow money for the purposes of the corporation does not include the power to issue ordinary irredeemable preferred stock for the purpose of raising money, for, as was said by the New York court of appeals, "the idea of a borrowing is not filled out unless there is in the agreement therefor a promise or understanding that what is borrowed will be repaid or returned, the thing itself or something like it of equal value, with or without compensation for the use of it in the meantime," and the issue of preferred stock cannot be looked upon "as other than a preference of one class of stockholders to another; as giving to the first class a perpetual, inextinguishable prior right to a portion of the earnings of the company before the other class might have anything therefrom." 611

It seems, however, that the power to borrow money may be relied upon as authorizing the issue of preferred stock, where the stock is redeemable by repayment of the money, and is issued merely as security for such repayment.<sup>612</sup>

(d) Extent of power.—When the charter or articles of asso-

<sup>608</sup> In re South Durham Brewery Co., 31 Ch. Div. 261, and other cases in note 606, supra.

<sup>609</sup> Post, chapter xxiv.

<sup>78</sup> N. Y. 159; 2 Keener's Cas. 936.

<sup>611</sup> Kent v. Quicksilver Min. Co., 78 N. Y. 159, 2 Keener's Cas. 936. 612 West Chester & Philadelphia R. Co. v. Jackson, 77 Pa. St. 321; Totten v. Tison, 54 Ga. 139; Hazlehurst v. Savannah, Griffin & N. A. R. Co., 43 Ga. 13.

ciation authorize the issue of preferred stock generally, and without limitations, it may be issued as a majority of the stockholders may determine, and there may be more than one issue. provided no contract rights are violated; but when the power is limited, the corporation cannot exceed the limitation. Thus, where the articles of a company authorized it to issue a certain number of shares each of preferred and common stock, specifying the amount of each, and then provided that additional stock might be issued, it was held that the corporation, on increasing its capital stock, could not issue the increased stock as second preferred, against the dissent of the common stockholders, even though the articles authorized the corporation to determine the conditions upon which stock should be issued, since to allow this would put it in the power of the corporation to utterly annihilate the interests of the common stockholders. 613

If the charter or articles of a corporation or a valid by-law provides that an increase of the capital stock may be made in such manner, and with such rules, regulations, privileges, and conditions as the stockholders may determine at a corporate meeting, the capital stock may be increased by issuing preferred stock.614

(e) Remedies of stockholders.—If the directors or a majority of the stockholders of a corporation threaten to issue or issue preferred stock without authority, a dissenting and nonparticipating stockholder, if he proceeds promptly, may maintain a suit in equity to enjoin the issue, or to cancel it, provided rights of innocent third persons have not intervened. 615 But his right

(N. S.) 578, 29 L. T. (N. S.) 364. "If they could issue one share," said Vice-Chancellor Malins in this case, "they could issue a thousand, L. R. 19 Eq. 358. and if at seven per cent., they might issue them at seventy per

613 Melhado v. Hamilton, 28 L. T. upon every principle of right between man and man, I think ought not to be." 28 L. T. (N. S.) 580.

614 Harrison v. Mexican Ry. Co.,

615 Kent v. Quicksilver Min. Co., cent.; and thus, at a general meet- 78 N. Y. 159, 2 Keener's Cas. 936; ing, they might pass resolutions Ernst v. Elmira Municipal Imp. which would have the effect of ut-Co., 24 Misc. Rep. (N. Y.) 583; terly annihilating the interests of Moss v. Syers, 32 L. J. Ch. 711. the ordinary shareholders. That, Compare Fielden v. Lancashire &

to such relief may be barred by laches. 616 or he may be estopped to object, as against creditors, and even as against the corporation and the stockholders, by having participated or acquiesced in the issue of the stock.617

# Effect of unauthorized issue or agreement to issue without authority.

As a general rule, a person who subscribes for or purchases preferred stock issued without authority,—at least where the issue does not amount to an overissue of stock,618—and who participated in the issue, or who has acted upon it as valid, as by voting it, receiving dividends, etc.,—cannot afterwards assert its invalidity and recover what he paid therefor, or escape liability to creditors on the corporation becoming insolvent. He is estopped. 619

Where a person subscribed for shares of preferred stock issued without authority, and was afterwards elected and acted

Yorkshire Ry. Co., 2 De Gex & S.

616 Kent v. Quicksilver Min. Co., 78 N. Y. 159, 2 Keener's Cas. 936; Taylor v. South & North Alabama R. Co., 4 Woods, 575, 13 Fed. 152; Branch v. Jesup, 106 U. S. 468; Higgins v. Lansingh, 154 III. 301; Hazlehurst v. Savannah, Griffin & N. A. R. Co., 43 Ga. 13; Andrews v. Gas Meter Co., [1897] 1 Ch. Div. 361, overruling Hutton v. Scarborough Cliff Hotel Co., 2 Drew & S. 514, 521, 4 De Gex, J. & S. 672, 2 Keener's Cas. 921.

617 See Branch v. Jesup, 106 U.S. 468; Banigan v. Bard, 134 U. S. 291, affirming 39 Fed. 13.

618 If the issue of preferred stock increases the amount of the capital stock beyond the amount authorized by the charter of the corporation, it is subject to the same rules as any other overissue of stock. See ante, § 407(g).

v. Jesup, 106 U. S. 468. Compare of the stock was unauthorized.

American Tube Works v. Boston Machine Co., 139 Mass. 5, as to which, see post, § 421, note 685.

In Branch v. Jesup, supra, it was held that, where preferred stock was issued by a corporation, neither the holders thereof nor their assignees, after having accepted the same, and received dividends or interest thereon for several years, could question the power of the corporation to issue it.

And in Banigan v. Bard, supra, it was held that an officer of a corporation who was a leader in its management, who was active in securing the passage of a resolution authorizing an issue of preferred stock, who subscribed for shares of the stock when issued, paid his subscription, took a certificate, and voted the stock at shareholders' meetings, and who induced others to take such stock, could not, on the corporation's becoming insolvent, recover back the 619 Banigan v. Bard, 134 U. S. money paid by him on his subscrip-291, affirming 39 Fed. 13; Branch tion, on the ground that the issue

as a director of the corporation, it was held that the stock might be treated as if it were common stock, and that he was liable upon it, as such, to creditors of the corporation. 620

Where a corporation borrowed money and agreed to repay the loan in preferred stock, when it had no power to issue such stock, it was held that the lender might maintain an action to recover the money, but in this case the issue of the stock was unauthorized, not because it was to be preferred stock, but because the issue would increase the capital stock beyond the amount fixed by its charter, and would therefore be an overissue. 621

Ratification.—An issue of preferred stock without authority from the stockholders may be rendered valid by ratification by them at a subsequent meeting.622

## § 417. Rights and remedies of preferred stockholders.

(a) In general.—The relation between a corporation and the holders of preferred stock therein is a contract relation, and the rights and remedies of the holders of such stock depend upon the express and implied terms of their contract. In the absence of special provisions, their rights are determined by certain well-settled rules, but the contract may be made subject to any special provisions that are not inconsistent with the charter or articles of association, nor contrary to law or public The terms of the contract are generally set forth in the certificates of the preferred stock issued to the holders as evidence of their shares, but they are not the only evidence of the contract. They must be read in connection with the provisions of the charter or articles of association, the general law, the by-laws in force at the time the stock was issued, except in so far as they may have been excluded, and the vote

<sup>620</sup> Tama Water-Power Co. v. Lockhart v. Van Alstyne, 31 Mich. Hopkins, 79 Iowa, 653. 76, 18 Am. Rep. 156, 2 Keener's 621 Anthony v. Household Sewing-Machine Co., 16 R. I. 571. 623 Heller v. National Marine

<sup>622</sup> In re London & New York Bank, 89 Md. 602, 73 Am. St. Rep. Inv. Corp., [1895] 2 Ch. Div. 860; 212.

or proceedings by or under which the stock was issued. All these enter into and form a part of the contract. 624

In determining whether a certificate is for preferred stock, and the terms of the contract, it is to be construed, not from its language alone, but in connection with the charter, articles of association, and by-laws of the corporation, and the proceedings of the corporation in issuing the stock.625

The calling of stock "preferred stock" does not per se define and fix the rights of the holders, whether it be so called by the corporation or by the legislature, but the rights depend upon the statute or contract under which it was issued. 626

(b) Change of contract or impairment of rights.—The contract between a corporation and the holders of its preferred stock cannot be changed, or their rights in any way impaired, without their consent, by any subsequent action of the corpora-Changes, however, may be made with the consent, express or implied, of the preferred stockholders, just as any other contract may be changed by mutual consent of the parties, and if a new arrangement is made by a majority of the

Co. v. City of Belfast, 77 Me. 445; a certificate of stock calling for a Heller v. National Marine Bank, ten per cent. dividend was prima 89 Md. 602, 73 Am. St. Rep. 212; facie evidence that the stock was Boardman v. Lake Shore & Michigan Southern Ry. Co., 84 N. Y. Boardman v. Lake Shore & Michier, 2 Keener's Cas. 1368; Rogers igan Southern Ry. Co., 84 N. Y. v. New York & Texas Land Co., 134 N. Y. 197; Gordon's Ex'rs v. Richmond, Fredericksburg & P. R. Co., 78 Va. 501, 2 Keener's Cas. 1384.

A by-law of a corporation is a contract between the corporation and its stockholders when it states the conditions upon which dividends are to be paid as between

preferred stock guarantying a dividend of ten per cent., it was held St. 116. that, in the absence of any evidence

624 Belfast & Moosehead Lake R. of the issue of other similar stock, igan Southern Ry. Co., 84 N. Y. 157, 2 Keener's Cas. 1384.

626 Heller v. National Marine Bank, 89 Md. 602, 73 Am. St. Rep.

"To call a thing by a wrong name does not change its nature. A mortgage creditor, although denominated a 'preferred stockholdpreferred and unpreferred stock. theless; and interest is not chang-Hazeltine v. Belfast & Moosehead ed into a 'dividend' by calling it Lake R. Co., 79 Me. 411, 1 Am. St. a dividend. Nothing is more com-Rep. 330; Belfast & Moosehead mon in the construction of stat-Lake R. Co. v. City of Belfast, 77 utes and contracts there are the statement of the statement 625 Where a corporation issued misnomers by supplying the proper words." Burt v. Rattle, 31 Ohio

627 See Ashbury v. Watson, 30

stockholders, a preferred stockholder who accepts the benefit thereof impliedly consents.628

(c) Whether the relation of preferred stockholders is that of stockholders or creditors-General rule.-In the absence of special provisions, the holders of preferred stock in a corporation are in precisely the same position, both with respect to the corporation itself and with respect to creditors of the corporation. as the holders of common stock, except only that they are entitled to receive dividends on their shares, to the extent guarantied or agreed upon, before any dividends can be paid to the holders of common stock. They are stockholders in the corporation, with all the rights and subject to the liabilities of stockholders, except in so far as there may be valid provisions in their contract to the contrary, and are not in the position of creditors of the corporation, 629 except in a limited and peculiar sense 630

It is no doubt safe to say that a corporation cannot, without express authority from the legislature, issue preferred stock

troit & Milwaukee Ry. Co., 8 Mich. 100; Campbell v. American Zylonite Co., 122 N. Y. 455; Pronick v. Spirits Distributing Co., 58 N. J. Eq. 97; West Chester & Philadelphia R. Co. v. Jackson, 77 Pa. St. 321: Hazeltine v. Belfast & Moosehead Lake R. Co., 79 Me. 411, 1 Am. St. Rep. 330.

N. Y. Supp. 722, 128 N. Y. 537.

629 Belfast & Moosehead Lake R. Co. v. City of Belfast, 77 Me. 445; Taft v. Hartford, Providence & F. R. Co., 8 R. I. 310, 5 Am. Rep. 575, 1 Smith's Cas. 347; Miller v. Ratterman, 47 Ohio St. 141; Warren v. King, 108 U.S. 389; Hamlin v. Continental Trust Co. of City of New York, 47 U.S. App. 422, 78 Fed. 664; Williston v. Michigan Southern & Northern Indiana R. Co., 13 Allen (Mass.) 400; Heller v. National Marine Bank, 89 Md. 602, 73 Am. St. Rep. 212; People v. St. Louis, Alton & T. H. R. Co., 176 Ill. 512: Chaffee v. Rutland R. Co.,

Ch. Div. 376; McLaughlin v. De- 55 Vt. 110; Field v. Lamson & Goodnow Mfg. Co., 162 Mass. 388: Birch v. Cropper, 14 App. Cas. 525.

Holders of preferred nonvoting stock, the certificates of which recite that it is a lien on the company's property, and entitled to interest payable only out of net earnings, and not to accumulate, are not creditors of the company, 628 Compton v. The Chelsea, 13 but stockholders, entitled to a preference over common stockholders as to dividends and capital. Hamlin v. Continental Trust Co. of City of New York, 47 U.S. App. 422, 78 Fed. 664.

> The fact that holders of preferred stock were formerly creditors of the corporation gives them no rights as against creditors, for, in abandoning their position as creditors, and becoming preferred stockholders, they lose their rights as creditors, and they cannot be reinstated in their former position. Warren v. King, 108 U. S.

630 "To be strictly accurate, we

which will give the holders the rights of stockholders, and also give them a claim for dividends or principal which will be superior to the right of creditors of the corporation to have its assets applied in payment of their claims. Such an arrangement, unless authorized by statute, would be contrary to public policy. In a late case in the federal circuit court of appeals. where certificates of preferred stock recited that they were a lien on the company's property, it was held that the holders were stockholders, and not creditors. "If the purpose," said the court, "in providing for these peculiar shares was to arrange matters so that under any circumstances a part of the principal of the stock might be withdrawn before the full discharge of all corporate debts, the device would be contrary to the nature of capital stock, opposed to public policy, and void as to creditors affected thereby."631

-But they may be creditors and be given a lien.—If authorized, however, a corporation may, in order to raise money, issue certificates in the form of certificates of preferred stock, so called, as security, making the holders creditors of the corporation, instead of mere stockholders, and even giving them a lien upon the property of the corporation, which will be superior to the rights of subsequent creditors or mortgagees.\* In a late Maryland case, a statute provided that any corporation

ought to say there is a sense in which a shareholder is a creditor. In that sense every corporation includes its capital stock amongst its liabilities, but it is a liability which is postponed to every other liability. And as to the matured

v. Toledo, St. Louis & K. C. R. Co., Building Co. v. Silverberg, 108 Ga. 72 Fed. 92.

\*An instrument purporting to entitle the holder to one share of preferred stock, but expressly depriving him of the right to vote at stockholders' meetings, providing that the amount specified therein should be paid by a certain day, with the right to pay before, and and unpaid guarantied dividends due on preferred stock, the relation of creditor undoubtedly exists." Per McSherry, C. J., in fore a certain day, by giving notheller v. National Marine Bank, tice, was held to be a certificate of indebtedness, and not a certificate of indebtedness, and not a certificate of professors. of preferred stock, although it pro-Co. of City of New York, 47 U. S. per cent. before payment of any App. 422, 78 Fed. 664. See, also, dividends to common stockholders. Continental Trust Co. of New York Savannah Real Estate, Loan &

having power to issue bonds as evidences of indebtedness, and to secure the same by a mortgage of its property, or having the power to obtain money upon mortgage, might, instead of doing so, issue a preferred stock, and execute an agreement under seal, acknowledged like conveyances of land, and recorded as therein provided, guarantying to the purchasers or subscribers for such stock a perpetual six per cent. dividend out of the profits of the corporation, payable before any dividends on other stock: that the holders of such stock should "have all the incidents, rights, privileges, and immunities, and liabilities, to which the capital stock of said corporation, or the holders thereof, may be entitled or subject;" and that "the said preferred stock shall be and constitute a lien on the franchises and property of such corporation, and have priority over any subsequently created mortgage, or other incumbrance." It was held that the statute was valid, and that by virtue thereof stock so created and issued made the holders creditors, instead of ordinary preferred stockholders, and gave them, upon the insolvency of the corporation, a valid lien on the franchises and property of the corporation superior to any subsequent mortgage, and to any unsecured claims which mortgages would have preference over.632 Such stock, of course, is not ordinary preferred stock, nor, technically, is it preferred stock at all, and therefore it is not governed by the ordinary rules. It is sui generis, and the rights of the holders are determined by the statute.633

When preferred stock, so called, is issued merely as a means of borrowing money, the corporation may secure the same by mortgage, thereby putting the holders in the position of secured creditors. In a leading Georgia case, a manufacturing company was authorized to borrow money and secure the loan by a mortgage of its property. To effect the loan, certificates of stock were prepared, bearing an indorsement that they rep-

<sup>632</sup> Heller v. National Marine Bank, 89 Md. 602, 73 Am. St. Rep. Bank, 89 Md. 602, 73 Am. St. Rep. 212.

resented preferred stock, with a guaranty of fifteen per cent. annually, for two years, when they were to be redeemed or converted into common stock at the option of the holder, and also that they were to be secured by first-mortgage bonds of the same amount held as collateral in the hands of trustees. loan was obtained by selling these certificates at par, secured by mortgage as stipulated. After the expiration of two years, the company being unable to pay the certificates, they were, by agreement with the company, exchanged by the holders for the mortgage bonds, which were delivered to the holders, and the scrip for the stock surrendered and cancelled. The holders of these certificates never took any part or voted in any of the meetings of the company, nor were they ever entered on the books as stockholders, and the amount of scrip issued to them did not make the stock of the company in excess of what is was authorized to issue. By all the resolutions of the directors, and of the stockholders, in reference to the transaction, it was recognized and ordered, as a means adopted to effect the loan which the company was authorized to effect, and there was nothing to show any fraud as against other creditors. Under these circumstances, it was held that, in a contest between creditors of the corporation on its insolvency over its assets, the holders of the mortgage bonds were entitled to claim as bona fide creditors.634

634 Totten v. Tison, 54 Ga. 129. modifying 86 Fed. 929.

Home Ins. Co. of Newark, 33 N. J. A provision in certificates of preferred stock issued by a railroad holders were, by their contract, company, making such stock a lien, not only on the net earnings, but tion of capital, as against the comalso on the property of the common stockholders, but no lien as pany, is not illegal, as against the against creditors; Burt v. Rattle, holders of common stock, in the 31 Ohio St. 116, where a manufacabsence of any charter or statutory turing company issued certificates provision affecting it. Toledo, St. of preferred stock, so called, certi-Louis & K. C. R. Co. v. Continental fying that it guarantied to the Trust Co. (C. C. A.) 95 Fed. 497, holders the payment of certain semiannual dividends, and the final For other cases in which it is shown that preferred stockholders may be creditors, and may be secured by a lien, or given a preference in distribution of capital, as well as of profits, see McGregor v. semiannual dividence, and the mai payment of the entire amount at a specified time, with the right to convert such stock into common stock, and at the same time executed and delivered to a trustee well as of profits, see McGregor v.

Where it is provided that preferred stock shall "be and remain a first claim upon the property of the company after its indebtedness," it gives the holders no lien or claim on the property of the corporation as against subsequent mortgages, or as against existing or subsequent unsecured creditors, but merely gives them a lien as against common stockholders. 635

---Relation both as stockholders and creditors.--It has been said that a person cannot, by virtue of a certificate of preferred stock, be, at least as to the creditors of the corporation, both a stockholder and a creditor at the same time. And this is certainly true in the case of ordinary preferred stock. relation of a holder of preferred stock," it was said in an Ohio case, "is, in some of its aspects, similar to that of a creditor, but he is not a creditor save as to dividends after the same are Nor does he sustain a dual relation to the corporation. He is either a stockholder or a creditor; he cannot, by virtue of the same certificate, be both. If the former, he takes a risk in the concerns of the company, not only as to dividends and a proportion of assets on the dissolution of the company, but as to the statutory liability for debts in case the corporation becomes insolvent; if the latter, he takes no interest in the company's affairs, is not concerned in its property, or profits

issued, reciting that the stipulated Jackson, 77 Pa. St. 321. interest was a lien on all the propupheld by the court as against v. Eric Ry. Co., 10 Blatchf. 271, subsequent mortgagees and gen- Fed. Cas. No. 12,226, 22 Wall. 136, eral creditors, although it was not 2 Keener's Cas. 1348; Mercantile secured by any mortgage; Fitch v. Trust Co. v. Baltimore & Ohio R. Wetherbee, 110 Ill. 475, where it Co., 82 Fed. 360.

the holders of such certificates,—it being held in this case that the holders of such certificates did not undertaking to pay dividends on become stockholders or members of the corporation, but its creditors only; and that, as such, they stock was a good mortgage. And had a lien upon the mortgaged property superior to that of general creditors of the corporation water Navigation Co. 29 Ch. Div. eral creditors of the corporation, water Navigation Co., 39 Ch. Div. or of its assignees; Skiddy v. At1; Gordon's Ex'rs v. Richmond, lantic, Mississippi & O. R. Co., 3 Fredericksburg & P. R. Co., 78 Va. Hughes, 320, 355, Fed. Cas. No. 12,- 501, 2 Keener's Cas. 1384; West 922, in which preferred stock was Chester & Philadelphia R. Co. v.

635 Warren v. King, 108 U. S. erty of the corporation after a 389; King v. Ohio & Mississippi R. first mortgage, and the lien was Co., 2 Fed. 36. See, also, St. John

as such, but his whole right is to receive agreed compensation for the use of money he furnishes, and the return of the principal when due. Whether he is one or the other depends upon a proper construction of the contract he holds with the company."636

As we have seen, however, this may not be true under particular statutory provisions. The legislature may expressly authorize the issue of stock which will give the holders the rights of creditors, and a lien on the property of the corporation which will have priority over the claims of subsequent creditors, and at the same time give them all the incidents, rights, privileges, and immunities, and subject them to all the liabilities, to which the ordinary stock of the corporation, or the holders thereof, are entitled or subject.637

- (d) Right to certificate.—A purchaser of or subscriber for preferred stock has the same right as a holder of common stock to a certificate of stock as evidence of his rights, and he is entitled to a certificate showing that his stock is preferred. the corporation refuses to issue such a certificate, mandamus will lie to compel it to do so,638 or the person entitled thereto may recover damages. 639
- (e) Rights with respect to dividends.—The holders of preferred stock are entitled to be paid dividends, in accordance with the terms of their contract, before any dividends can be paid to the holders of common stock.640 The amount of the preference depends, of course, upon the terms upon which the stock is issued. Except as to this right of priority over common stock, preferred stock is subject, in so far as the payment of dividends is concerned, to substantially the same rules as common stock, unless they are rendered inapplicable by express provision. Thus, dividends on ordinary preferred stock, like

St. 141. And see Hamlin v. Con-tinental Trust Co. of City of New York, 47 U. S. App. 422, 78 Fed. 644; Heller v. National Marine Bank, 89 Md. 602, 73 Am. St. Rep. 212. 687 Heller v. National Marine

<sup>636</sup> Miller v. Rotterman, 47 Ohio Bank, 89 Md. 602, 73 Am. St. Rep.

<sup>638</sup> State v. Cheraw & Chester R. Co., 16 S. C. 524. See post, § 425. 639 Post, § 425.

<sup>640</sup> Post. § 529.

dividends on common stock, are payable, even when they are guarantied, only when there are net earnings or surplus profits out of which dividends may properly be paid. If there are no such earnings or profits, preferred stockholders are not only not entitled to dividends, but it is a fraud upon creditors and illegal for the corporation to pay them.<sup>641</sup>

In the absence of some express provision, holders of preferred stock have no rights against the corporation, by way of lien or otherwise, superior to the lien of mortgage bondholders.<sup>642</sup> It may be otherwise, of course, under special provisions making the holders of preferred stock creditors, and not mere stockholders, and giving them a lien, as for interest, or authorizing payment of the stipulated dividend out of gross earnings, etc.<sup>643</sup>

The right to dividends on preferred stock, the remedies of preferred stockholders, whether dividends are cumulative, so as to entitle the holders to payment of arrears, and other questions, will be considered at length in a subsequent chapter treating generally of dividends.<sup>644</sup>

When a corporation which has issued preferred stock is consolidated with another corporation, and the consolidated corporation assumes all its liabilities, it is liable for dividends due on the stock.<sup>645</sup>

(f) Rights as to management of corporation.—Preferred stock-holders have the same rights with respect to the management of the corporation as the common stockholders, 646 except in so far as they may be excluded by their contract. 647 Their con-

641 Taft v. Hartford, Providence & F. R. Co., 8 R. I. 310, 5 Am. Rep. 575, 1 Smith's Cas. 347; Lockhart v. Van Alstyne, 31 Mich. 76, 18 Am. Rep. 156, 2 Keener's Cas. 1354; Field v. Lamson & Goodnow Mfg. Co., 162 Mass. 388; Miller v. Rotterman, 47 Ohio St. 141; post, § 529.

642 Mercantile Trust Co. v. Baltimore & Ohio R. Co., 82 Fed. 360. See supra, this section, (c).

643 See Skiddy v. Atlantic, Mississippi & O. R. Co., 3 Hughes, 355,Fed. Cas. No. 12,922 (note 634,

supra); Gordon's Ex'rs v. Richmond, Fredericksburg & P. R. Co., 78 Va. 501, 2 Keener's Cas. 1384. And see supra, this section, (c).

644 Post, § 529.

645 Chase v. Vanderbilt, 62 N. Y. 307; Boardman v. Lake Shore & Michigan Southern Ry. Co., 84 N. Y. 157, 2 Keener's Cas. 1368.

646 Thompson v. Erie Ry. Co., 42
 How. Pr. (N. Y.) 68, 11 Abb. Pr.
 (N. S.; N. Y.) 188.

647 Miller v. Ratterman, 47 Ohio St. 141; infra, this section, (g).

tract may give them greater rights;648 but, in the absence of express provision to the contrary, their rights are the same. With the exception that they may interfere and maintain proper suits against and on behalf of the corporation, in a proper case, to protect their rights as preferred stockholders, they cannot interfere in any case in which a holder of common stock would have no right to interfere.649 "Holders of 'preferred stock,' have no special control over the corporation or its management. Stockholders are the constituent elements of a corporation, and in this case there is no other difference between the two classes than this: one is to be paid interest out of a certain fund, if raised, to the exclusion of the other, if such fund is inadequate to pay both. The corporation is in no sense the trustee for the holders of preferred stock. Its duty is to each alike according to the conditions attached to the stock of each."650

(g) Right to vote at corporate meetings.—In the absence of charter or statutory provision or valid stipulation to the contrary, holders of preferred stock have the same right as holders of common stock to vote at stockholders' meetings.651 their contract may even give them the right to vote to the exclusion, for a time, of the holders of common stock, so as to place the management of the corporation entirely in their hands for the time specified. 652 On the other hand, it is within the power of a corporation, when it issues preferred stock, to provide expressly that it shall give no right to vote, and when the certificates contain such a provision, it will be binding upon all persons who accept the same. 653

Marquette R. Co., 32 Fed. 350, 34 er's Cas. 1354.

<sup>649</sup> Mackintosh v. Flint & Pere Marquette R. Co., 32 Fed. 350, 34 Ted. 582; Thompson v. Erie Ry. Co., 42 How. Pr. (N. Y.) 68, 11 Abb. Pr. (N. S.; N. Y.) 188. 650 Thompson v. Erie Ry. Co., 42

How. Pr. (N. Y.) 68, 11 Abb. Pr. 47 U. S. App. (N. S.; N. Y.) 188. In re Barrow H 651 Lockhart v. Van Alstyne, 31 39 Ch. Div. 582.

<sup>648</sup> Mackintosh v. Flint & Pere Mich. 76, 18 Am. Rep. 156, 2 Keen-

<sup>652</sup> Mackintosh v. Flint & Pere Marquette R. Co., 32 Fed. 350, 34 Fed. 582.

<sup>653</sup> Miller v. Ratterman, 47 Ohio St. 141; Hamlin v. Continental • Trust Co. of City of New York, 47 U. S. App. 422, 78 Fed. 664; In re Barrow Haematite Steel Co.,

(h) Rights on distribution of assets on insolvency or dissolution.—When the assets of a corporation are distributed among its stockholders, not by way of dividend, but on a dissolution and winding up, the holders of preferred stock have the same, and no greater, right to share in the assets as the holders of common stock,654 unless, by statute or by their agreement with the corporation, they are given a preference, not only in the payment of dividends, but also in the distribution of capital.655

Since the holders of ordinary preferred stock are stockholders, and not creditors of the corporation, they are not entitled, any more than the holders of common stock, to receive any portion of the assets of the corporation, on its insolvency or dissolution, until the creditors of the corporation are fully paid. "The law is perfectly well settled that as between creditors and ordinary preferred stockholders, the latter, as owners 656 of the property of an insolvent corporation, are, upon a distribution of its assets, entitled to nothing until its creditors are first fully There is a palpable difference between the relation of a stockholder and a creditor to the corporate property. Stock, whether preferred or common, is capital; and generally speaking, a certificate of stock merely evidences the amount which the holder has contributed to or ventured in the enterprise. . Such a certificate, representing nothing more than the extent of his ownership in the capital, cannot well be treated as indi-

654 Jones v. Concord & Montreal such stock, and that they had no R. R., 67 N. H. 119, 234, 68 Am. St. Rep. 650; Birch v. Cropper, 14 App. Cas. 525; Gordon's Ex'rs v. Richmond, Fredericksburg & P. R. Co., 78 Va. 501, 2 Keener's Cas. 1384.

It was held, for this reason, no greater right than the common Ohio St. 141. stockholders in the distribution of

greater right than the common stockholders, therefore, to preferred stock in the new company. Simpson v. Palace Theatre, 69 L. T. (N. S.) 70.

655 Hamlin v. Continental Trust Co. of City of New York, 47 U.S. where the property of a corpora- App. 422, 78 Fed. 664; Continental tion was transferred to a new cor- Trust Co. v. Toledo, St. Louis & K. poration, on a reorganization, and C. R. Co., 86 Fed. 929; Heller v. preferred and common stock of the National Marine Bank, 89 Md. 602, new company was taken in pay- 73 Am. St. Rep. 212; McGregor v. ment, that the preferred stock- Home Ins. Co. of Newark, 33 N. J. holders of the old company had Eq. 181; Miller v. Ratterman, 47

656 Equitable owners.

cating that he is, by virtue of it alone, also to the same extent a creditor who may compete with other creditors in the distribution of the fund arising from a conversion of the corporation's assets into money. He cannot, if he is simply an ordinary preferred stockholder, in the nature of things, so far as third persons are concerned, be at one and the same time and by force of the same certificate, both part owner of the property and creditor of the company for that portion of its capital which stands in his name. His certificate, therefore, in such circumstances, merely measures the quantum of his ownership. As his chance of gain throws on the stockholder, as respects creditors, the entire risk of the loss of his contribution to the capital, it is a fixed characteristic of capital stock that no part of it can be withdrawn for the purpose of repaying the principal of the capital until the debts of the corporation are satisfied "657

As we have seen, however, the holders of preferred stock, so called, may be given a prior lien by or under express statutory provision.658 And when a dividend upon preferred stock has been lawfully declared out of profits, but not paid, the holders have the rights of creditors, as distinguished from stockholders, to the extent of such dividend.659

(i) Rights on increase or reduction of capital stock.-When a corporation increases its capital stock, holders of preferred stock have the same privilege as holders of common stock to subscribe for or purchase a proportionate amount of the new stock, unless there is some provision to the contrary in their contract; and it makes no difference that the amount of dividends is limited.660

In like manner, on a reduction of the capital stock because of losses, preferred stock must be reduced proportionately with

<sup>657</sup> Heller v. National Marine Bank, 89 Md. 602, 73 Am. St. Rep. Bank, 89 Md. 602, 73 Am. St. Rep. 212. 212, McSherry, C. J. See, also, Hamlin v. Continental Trust Co. of City of New York, 47 U. S. App. 422, 78 Fed. 664.

<sup>659</sup> See post, § 527(c).

<sup>660</sup> Jones v. Concord & Montreal R. R., 67 N. H. 119, 234, 68 Am. St. 658 Heller v. National Marine Rep. 650.

common stock unless there is some special provision in the statute or contract of the parties fixing a different rule. 661 rule does not apply where the stock is preferred, not merely as to dividends, but also as to capital.662

(j) Preferred stock convertible into bonds.—A corporation may be authorized to issue preferred stock convertible into mortgage bonds of the corporation at the option of the holders. the corporation wrongfully refuses to convert the stock into bonds on request of the holder, he may maintain an action of general assumpsit, and recover the amount of his certificates. 663

## § 418. Liabilities of preferred stockholders.

In the absence of express provision to the contrary, the holders of preferred stock in a corporation are subject to the same liabilities as the holders of the common stock. Thus they are liable on the same principles upon their subscriptions for shares. And creditors, if the corporation becomes insolvent, may in equity compel subscribers to pay the full amount of their subscriptions, irrespective of any secret agreements with the corporation. 664 So, where a statute makes the stockholders of a corporation individually liable to creditors beyond the par value of their shares, it applies to the holders of preferred stock.665

# § 419. Rights of common stockholders.

(a) In general.—The rights and remedies of common stockholders where an issue of preferred stock is unauthorized have been shown in a previous section.<sup>666</sup> When the issue of pre-

661 In re Quebrada Railway, Land 1 Ch. Div. 396; In re London & Copper Co., 40 Ch. Div. 363; New York Inv. Corp., [1895] 2 Ch. & Copper Co., 40 Ch. Div. 363; Bannatyne v. Direct Spanish Telegraph Co., 34 Ch. Div. 287; In re Barrow Haematite Steel Co., 39 Ch. Div. 582; In re Gatling Gun, 43 Ch. Div. 628.

662 In re Quebrada Railway, Land & Copper Co., 40 Ch. Div. 363; In re Agricultural Hotel Co., [1891] Div. 860.

668 Chaffee v. Rutland R. Co., 55 Vt. 110. See post, § 422.

664 See post, chapter xxv.

665 Railroad Co. v. Smith, 48 Ohio St. 219.

666 Ante, § 416.

ferred stock is valid as against them, any rights which they would ordinarily have as stockholders are subordinated to the rights given to the preferred stockholders by their contract.667 As has been stated, they have no right to dividends until the stipulated dividend has been paid on the preferred stock.668 They may be given the right to vote at corporate meetings, to the exclusion of the preferred stockholders, or, on the other hand, they may be deprived of the right to vote.669

A holder of common stock cannot prevent contracts or leases, etc., by the corporation, which are within the powers conferred upon it, expressly or impliedly, by its charter, although the result of such contracts, leases, etc., may be to leave nothing for them after the payment of the dividends on the preferred But they can object to and prevent any arrangement or transaction entered into or threatened by the company for the purpose of putting the preferred stockholders on a more favorable footing than is secured to them by their contract. 671

(b) Exchange of common for preferred stock.-When a corporation is authorized to issue preferred stock, and there is no charter or statutory provision in the way, it may lawfully exchange preferred stock for common stock, provided all the stockholders are given the same right and opportunity to make the exchange. 672 When an offer to exchange preferred for common stock is made, stockholders must exercise the option, and notify the corporation within the time, if any, specified in the offer, or within a reasonable time, if no time is specified. 673

# § 420. Interest bearing stock.

A corporation has the same power to issue stock under an

<sup>667</sup> Ante, § 529.

<sup>668</sup> Ante, § 417(e). 669 Ante, § 417(g).

<sup>670</sup> In re Buenos Ayres Water

Supply & Drainage Co., 66 L. T. (N. S.) 408; Town of Middletown v. Boston & New York Air Line R. Co., 53 Conn. 351.

<sup>671</sup> Phillips v. Eastern R. Co., 138

<sup>672</sup> Pearson v. London & Croydon Ry. Co., 14 Sim. 541; Holland v. Cheshire R. Co., 151 Mass. 231.

<sup>673</sup> Pearson v. London & Croydon Ry. Co., 14 Sim. 541; Holland v. Cheshire R. Co., 151 Mass. 231. And see post, § 422.

agreement to pay a certain rate of interest thereon as it has to issue ordinary preferred stock. 674 Such stock, called "interest bearing stock," is in effect preferred stock entitling the holders to the payment of the stipulated interest before payment of dividends to common stockholders, and gives the holders the same rights as stockholders, and renders them subject to the same liabilities as stockholders, as ordinary preferred stock would.675 The interest cannot be lawfully made payable or paid except out of net earnings or surplus profits available for the payment of dividends. 676

A railroad company, to induce the payment of money on subscriptions, may agree to pay interest on all sums paid in on subscription until the road is put in operation, or until it is wholly or partly constructed.677

# § 421. "Special stock" under Massachusetts statute.

In a sense, preferred stock, or any stock other than ordinary stock, may be called "special stock," but the expression is used

674 McLaughlin v. Detroit & Milwaukee Ry. Co., 8 Mich. 100; Barnard v. Vermont & Massachusetts
R. Co., 7 Allen (Mass.) 512; Richardson v. Vermont & Massachusetts
when it should be able, and the
ardson v. Vermont & Massachusetts R. Co., 44 Vt. 613; Miller v.
Pittsburgh & Connellsville R. Co., Massachusetts R. Co., 7 Allen
40 Pa. St. 237. See, also, City of (Mass.) 512.
Ohio v. Cleveland & Toledo R. Co.,
6 Ohio Cleveland & Toledo R. Co.,
6 Ohio Cleveland & College of field R. Co. 8 Gray (Mass.) 433: 6 Ohio St. 489; Ohio College of field R. Co., 8 Gray (Mass.) 433; Dental Surgery v. Rosenthal, 45 Milwaukee & Northern Illinois R. Ohio St. 183.

675 McLaughlin v. Detroit & Milwaukee Ry. Co., 8 Mich. 100.

676 Pittsburg & Connellsville R. Co. v. County of Allegheny, 63 Pa. St. 126; Barnard v. Vermont & Massachusetts R. Co., 7 Allen (Mass.) 512; Cunningham v. Vermont & Massachusetts R. Co., 12 Gray (Mass.) 411; Painesville & Hudson R. Co. v. King, 17 Ohio St. 534; Richardson v. Vermont & Massachusetts R. Co., 44 Vt. 613; Lockhart v. Van Alstyne, 31 Mich. Assur. Co., 10 Ch. Div. 118.

As to compelling a corporation

Milwaukee & Northern Illinois R. Co. v. Field, 12 Wis. 340; Racine County Bank v. Ayres, 12 Wis. 512; Miller v. Pittsburgh & Connellsville R. Co., 40 Pa. St. 237.

post, § 467(d).

Where a railroad company agreed that a subscriber for its stock should have the privilege of paying in at any time the whole or any part of his subscription, and that he should receive interest thereon until the road should go into operation, it was held that the company was not bound to pay any interest until the road went 76, 18 Am. Rep. 156, 2 Keener's into operation. Waterman v. Troy Cas. 1354; In re National Funds & Greenfield R. Co., 8 Gray (Mass.) 433.

here with reference to a kind of stock which is issued under a Massachusetts statute, and so called. In that state it is provided that manufacturing and certain other corporations may, by a vote of three-fourths of the general stockholders, at a meeting duly called for the purpose, issue special stock, which shall at no time exceed two-fifths of the actual capital, and which shall be subject to redemption at par after a fixed time, to be expressed in the certificates; and that holders of such stock shall be entitled to receive, and the corporation shall be bound to pay thereon, a fixed half-yearly sum or dividend, to be expressed in the certificates, not exceeding four per cent., and shall in no event be liable for the debts of the corporation beyond their stock.<sup>678</sup> The special stock so authorized is not the same as preferred stock, but is sui generis,—"a peculiar kind of stock, distinctly provided for by statute,"679 and a vote to issue such stock at a meeting called to consider whether "preferred stock" shall be issued is invalid.680

The obligation to pay the dividends guarantied is not dependent, as in the case of preferred stock, upon there being net earnings or surplus profits, but is absolute, and renders the corporation the debtor of the holders.<sup>681</sup>

In issuing such stock, the statutory provisions must be substantially complied with. There must be a meeting of the stockholders, as required by the statute, called for the purpose of issuing such stock; 682 and it must affirmatively appear from the records of the meeting that the issue was voted for by at least three-fourths of the general stockholders of the corporation, as required by the statute. 683 A holder of certificates of special stock which is illegally issued cannot, by estoppel or

<sup>678</sup> Pub. St. Mass. 1882, c. 106, §§ 681 Williams v. Parker, 136 Mass. 42, 61, cl. 3. And see Laws 1886, 204, 2 Keener's Cas. 1381.

<sup>679</sup> Per C. Allen, J., in American 688 American Tube Works v. Bos-Tube Works v. Boston Machine ton Machine Co., 139 Mass. 5. Co., 139 Mass. 5.

<sup>680</sup> American Tube Works v. 683 American Tube Works v. Bos-Boston Machine Co., 139 Mass. 5. ton Machine Co., 139 Mass. 5.

otherwise, become a stockholder with respect to such shares,684 and if the stock is illegally issued, so that it is void, he may rescind and recover what he has paid therefor. 685

VII. BONDS, ETC., CONVERTIBLE INTO STOCK, AND STOCK CONVERTIBLE INTO BONDS, OR LAND, ETC.

In general.—When a corporation issues stock convertible into bonds or land, or bonds convertible into stock, etc., at the option of the holder, the rights of the holder are determined by the terms of the contract. He must exercise the option within the time, if any, specified, or, if no time is specified, within a reasonable time.

If the corporation refuses to make the exchange the holder may maintain assumpsit or covenant, according to the circumstances, to recover damages, or he may sue in equity for specific performance.

A holder of notes or bonds convertible into stock is not a stockholder, nor entitled to rights as such, until he has exercised the option and received the stock.

A corporation is sometimes authorized to issue bonds or notes convertible into stock at the option of the holder, or to issue stock convertible into bonds, or, in the case of a land company, into land. And to some extent, no doubt, such power may be

684 American Tube Works v. Bos- titled to rescind, that the resciston Machine Co., 139 Mass. 5.

special stock in a corporation was corporation. illegally issued to a creditor of the corporation, who subsequently received dividends thereon, and the corporation, at two subsequent ceived, it was held that he was en- they were of no value.

sion was in time, and that he could 685 In American Tube Works v. prove the amount of his debt Boston Machine Co., supra, where against the insolvent estate of the

In Reed v. Boston Machine Co., 141 Mass. 454, where the plaintiffs had received special stock in a meetings attempted, but failed, to corporation, which was illegally cure the defect, and to make the issued, and which could not be issue of the stock valid, and twen- rendered valid by the corporation, ty-seven months after the first is- it was held that they might prove sue, and two months after the last against the insolvent estate of the attempt to cure the defect, the corporation for the amount paid creditor, shortly before the insolby them for the stock, with intervency of the corporation, gave noest, less dividends received by tice that he rescinded the contract, them, and that they need not reand tendered back the dividends return the certificates of stock, as

implied in the absence of express provision therefor.686 grant of such power carries with it by implication the power to do everything necessary to enable the corporation to exercise Thus, if a corporation is authorized to issue bonds convertible into stock, at the option of the holder, it is impliedly given the power to increase the amount of its capital stock to such an extent as may be necessary to make the exchange.687

When a corporation is prohibited by its charter from issuing stock at a discount, it cannot sell at a discount bonds convertible into stock 688

The rights and liabilities of the parties under such a contract depend, of course, upon the terms of the contract. corporation cannot be compelled to exchange stock for notes or bonds, as therein provided, prior to the time, if any, fixed by the contract, or on other terms than those prescribed. 689

If a bond is convertible into stock at the option of the holder. without any restriction as to time, he may exercise the option and demand the stock at any time within a reasonable time, and if he exercises the option and receives or demands the stock just before the declaration of a dividend, he will be entitled to the dividend, when declared, as well as the stock. 690 not entitled, however, to dividends declared prior to his demand for the stock. 691

Where an option is given to convert bonds into stock, or vice versa, or stock into land, etc., within a specified time, the limitation as to time is a term of the contract, and the corporation cannot be compelled to make the exchange unless the option

686 See Van Allen v. Illinois Central R. Co., 7 Bosw. (N. Y.) 515; Chaffee v. Rutland R. Co., 55 Vt. 110; Denney v. Cleveland & Pittsburg R. Co., 28 Ohio St. 108; Pratt v. American Bell Tel. Co., 141 Mass. 225, 55 Am. Rep. 465.

As to the estoppel of a corporation to deny the validity of certificates of stock convertible into mortgage bonds, see Chaffee v. Rut-

land R. Co., 55 Vt. 110.

687 Belmont v. Erie Ry. Co., 52 Barb. (N. Y.) 637; Ramsey v. Erie Ry. Co., 38 How. Pr. (N. Y.) 193.

688 Sturges v. Stetson, 1 Biss. 246, Fed. Cas. No. 13,568.

689 Pratt v. American Bell Tel. Co., 141 Mass. 225, 55 Am. Rep. 465. 690 Jones v. Terre Haute & Rich-

mond R. Co., 57 N. Y. 196.

691 Sutliff v. Cleveland & Mahoning R. Co., 24 Ohio St. 147.

is exercised and an exchange demanded within the time speci-If no time is specified within which the option must be exercised, a reasonable time is implied, for it is a general principle that, "where an option to be exercised or a condition to be performed is not limited by the agreement, such option must be acted upon and the condition performed or abandoned within a reasonable time."693

Persons holding bonds or notes of a corporation convertible into stock at their option are not in the position of stockholders, either at law or in equity, nor are they entitled to the rights of stockholders, until they have exercised the option and received the stock, or, at least, until the time fixed for exercise of the option, and a demand, but are merely creditors. 694 has been held, therefore, that until then they are not entitled to a stockholder's right of preference in subscribing for or purchasing new stock on an increase of the capital stock of the The same would be true of the right to divicorporation. 695 dends, the right to vote at corporate meetings, and other rights of stockholders.

If a corporation refuses to exchange bonds for stock, or stock for bonds, or land for stock, etc., in accordance with the terms of its contract, the holder may maintain an action of assumpsit or covenant, as the case may be.696 Or, in a proper case, he

on Ry. Co., 5 Hare, 519; Catlin v. Green, 120 N. Y. 441.

holders of loan notes of a corporation to exchange the same for shares of stock within a specified time, a holder of such notes cannot exercise the option after the time fixed, and compel the corporation to make the exchange, although he may have lived abroad, and been ignorant of the option until after the expiration of the See, also, Pearson v. London &

692 Campbell v. London & Bright- may be converted into stock is not extended by extension of the time of payment of the bond. Muhlen-When an option is given to the berg v. Philadelphia & Reading R. Co., 47 Pa. St. 16.

693 Catlin v. Green, 120 N. Y. 441. In this case, it was held that the owners of stock convertible into bonds at their option were chargeable with laches in the exercise of the option, and had waived all right to exercise the same.

694 Pratt v. American Bell Tel. Co., 141 Mass. 225, 55 Am. Rep. 465. time limited. Campbell v. London 695 Pratt v. American Bell Tel. & Brighton Ry. Co., 5 Hare, 519. Co., 141 Mass. 225, 55 Am. Rep. 465. 696 Where a corporation, having Croydon Ry. Co., 14 Sim. 541. issued certificates of stock con-The time within which a bond vertible into mortgage bonds, may maintain a suit in equity for specific performance.697 When a corporation has issued stock convertible into land, and the corporation refuses to perform its contract, the stockholder may maintain a suit in equity for specific performance. 698

If a corporation has no unissued stock, a holder of bonds or notes convertible into stock cannot maintain a suit for specific performance, since the court could not enforce specific performance, but his remedy is by an action to recover damages for breach of contract or covenant. 699

A stipulation in a bond of a corporation that it may be converted into stock is inseparably connected with the bond, and is only available to the holder of the bond, and so long only as he continues to hold the same. The holder of such a bond, therefore, cannot assign to another his right of action against the corporation for damages for breach of the stipulation, and yet retain the bond for the benefit of himself and his future assignees. 700 Nor can the holder of such a bond, after he has assigned the same to another, maintain an action against the corporation to recover damages for its refusal to exchange stock for the bond prior to the assignment.701

wrongfully refuses to make the exchange, or to pay the amount thereof, the holder may maintain general assumpsit for the amount of the certificates. Chaffee v. Rutland R. Co., 55 Vt. 110.

Where installments are still due on bonds convertible into stock, the measure of damages for the corporation's refusal to convert the same on demand is the difference between the market value of the stock at the time of the demand and the amount of the installments due and interest on such installments, with interest on such difference from the time of the demand to the day of the verdict. Van Allen v. Illinois Central R. Co., 7 Bosw. (N. Y.) 515.

Tel. Co., 141 Mass. 225, 55 Am. Rep.

698 Franco-Texan Land Co. v. Bousselet, 70 Tex. 422; Franco-Texan Land Co. v. Laigle, 59 Tex. 339.

As to bonds convertible into land, see Chicago & Great Western Railroad Land Co. v. Peck, 112 Ill.

699 Chaffee v. Middlesex R. Co., 146 Mass. 224.

700 Denney v. Cleveland & Pittsburg R. Co., 28 Ohio St. 108.

701 Denney v. Cleveland & Pittsburg R. Co., 28 Ohio St. 108.

It follows that a complaint in an action for such damages is fatally defective if it fails to aver that the plaintiff was, and at the commence-697 See Pratt v. American Bell ment of the action continued to be, the holder of the bond for the nonconversion of which he sues. Id.

When a corporation which has outstanding bonds convertible into stock is consolidated with another corporation, and the new corporation takes the property of the old, and expressly or impliedly assumes its liabilities, as explained in a former chapter, or if liability is imposed by statute, the consolidated corporation assumes the liability on the bonds, and the holders of the bonds may demand compliance with their provisions, and maintain an action against it to recover damages for breach of the contract, or, if the corporations have been consolidated on a footing of equality between the shares of their stock and the shares of stock in the new corporation, they may require the new corporation to deliver shares of its own stock, or pay damages for refusal to do so.702

VIII. ISSUE AND CANCELLATION OF CERTIFICATES OF STOCK; LOST CER-TIFICATES.

In general.—A corporation has the power to issue certificates of stock, subject to the restrictions in its charter; and a stockholder is entitled to a certificate as soon as he has paid for his stock, or before, if his contract makes him a stockholder before payment. If a corporation wrongfully refuses to issue a certificate, the person entitled may, by the weight of authority, compel it to do so by mandamus, or by suit in equity for specific performance; or he may maintain assumpsit to recover damages for its breach of contract; or, if he had title to the stock, he may treat the refusal of a certificate as a conversion of the stock, and maintain an action of trover; or a subscriber, except as against creditors after the corporation is insolvent, may rescind and recover what he has paid.

If a certificate of stock is lost or destroyed, the stockholder is entitled to a new certificate on giving a bond to indemnify the

702 John Hancock Mut. Life Ins. Co., 129 Mass. 170; Parkinson v. 702 John Hancock Mut. Life Ins. Co., 129 Mass. 170; Parkinson v. Co. v. Worcester, Nashua & R. R. West End Street Ry. Co., 173 Co., 149 Mass. 214; Day v. Worcester, Nashua & R. R. Co., 151 Central Ry. Co., 29 Md. 557; Ro-Mass. 302.

See, also, India Mut. Ins. Co. v. ton & M. Ry. Co., 18 Fed. 513; Worcester, Nashua & R. R. Co. Cayley v. Cobourg, P. & M. Railway (Mass.) 25 N. E. 975; Child v. & Mining Co., 14 Grant's Ch. New York & New England R. (Can.) 571. See ante, § 356(b)(3).

corporation against possible liability on the certificate alleged to be lost or destroyed, or, it seems, without giving indemnity, if it clearly appears that the certificate has in fact been destroyed, or actually stolen or lost, and in such condition that no liability can be incurred thereon.

A corporation may sue to cancel and enjoin the transfer of certificates which are void or voidable, and thus prevent them from getting into the hands of bona fide holders.

# § 424. Power to issue certificates of stock, and validity of certificates.

As was explained in a former section, a certificate of stock is a written instrument issued by a corporation to its stockholders as evidence of their ownership of stock. It is not the stock itself, nor, as a rule, is it necessary to render one a stockholder, but it is merely evidence of the holder's title and rights as a stockholder. 703 A joint-stock corporation undoubtedly has the power to issue certificates to its stockholders as evidence of their ownership of shares, except in so far as there may be restrictions in its charter or the general law. In the absence of restrictions, a corporation may issue a certificate of stock before the shares are paid for in full, or even before anything at all is paid, for payment of a subscription, unless expressly required, is not necessary to render one a stockholder.704 Where the charter, however, or a general law, expressly or by clear implication, requires that stock shall be paid up in full before the issue of a certificate therefor, the corporation cannot lawfully issue a certificate for stock which has not been fully paid for; and if it does so, the certificate is void, and confers no rights, 705 unless it has gotten into the hands of a bona fide purchaser for value. 706 Where a statute provided that certificates of stock should be issued "for all stock paid up, from time to time, in compliance with the requirements of such directors."

<sup>703</sup> Ante, § 378.
704 Green v. Abietine Medical 15, 99 Am. Dec. 237.
Co., 96 Cal. 322. See ante, §§

<sup>378(</sup>b), 383, and cases there cited. 706 See post, § 408 et seq.

or that might "be fully paid in advance of such requirements by the voluntary act of any stockholder," it was held that payment in full for stock was a condition precedent to the power to issue a certificate. 707 But in a later case in the same state it was held that a statute merely authorizing the issue of certificates when stock should be fully paid up did not prohibit the issue of the certificates before full payment.<sup>708</sup>

Of course a corporation has no power to issue certificates in excess of the amount of its authorized capital stock. If it does so, it may be liable in damages to bona fide purchasers of the pretended stock, 709 but, as was shown in a former section, the certificates are void, and neither confer rights nor impose liabilities as a stockholder.710

Certificates representing a fictitious increase of stock, in violation of a statutory or constitutional provision that no corporation shall issue stock except for money paid, labor done, or property actually received, and that all fictitious increase of stock shall be void, are void as between the corporation and the holder, and in some jurisdictions as between the holder and subsequent creditors of the corporation.<sup>711</sup> But undersuch a provision, where certificates of stock are merely in excess of the shares which are paid for, being fictitious only as to some of the shares represented thereby, the certificate is not wholly void. It is void only in so far as it represents fictitious stock. A note given for such a certificate, therefore, by a purchaser from the original holder, is supported by a sufficient consideration,712

<sup>15, 99</sup> Am. Dec. 237.

<sup>707</sup> Brewster v. Hartley, 37 Cal. fully paid up. Green v. Abietine 99 Am. Dec. 237. Medical Co., 96 Cal. 322, 330. 708 A statute (Civ. Code Cal. \$ 709 Post, \$ 428 et seq. 710 Ante, \$ 407(g). 708 A statute (Civ. Code Cal. § 323) providing that "all corporations for profit must issue certificates for stock when fully paid up, \* \* and may provide, in their such restrictions and for such purposes as their by-laws may pro- 395, 401. vide," does not prohibit the issue 712 Beitman v. Steiner Bros., 98 of certificates before the stock is Ala. 241.

<sup>711</sup> Jefferson v. Hewitt, 103 Cal. 624; Beitman v. Steiner Bros., 98 Ala. 241. This question has been by-laws, for issuing certificates fully considered in the sections reprior to the full payment, under lating to watered or fictitiously paid up stock. See ante, §§ 391.

In order that a certificate may be regarded as issued, so as to confer rights, when issue of a certificate is necessary, it must have been delivered.<sup>713</sup> Making out a certificate and mailing it to a stockholder is an issue thereof.714

Issue of a certificate of stock to a transferee of stock is one of the formalities in a transfer of stock,715 but the issue of a certificate to an original subscriber is in no sense a transfer of stock, and therefore it is not within a provision of the charter or by-laws that stock shall be transferable only on the books of the corporation.716

In issuing a certificate of stock, the corporation may insert therein any stipulation or provision which does not violate its contract with the stockholder, and which is not contrary to the provisions of its charter, or to the general law, and valid provisions or stipulations inserted therein will be binding upon the person to whom the certificate is issued, upon transferees thereof, and upon the corporation.717

With respect to form, certificates must comply with the provisions of the charter and valid by-laws. If they provide generally for certificates in a certain form, and signed by particular officers, all certificates, to whomsoever they may be

713 York v. Passaic Rolling-Mill Co., 30 Fed. 471.

Where a certificate of stock was drawn up for a person by a corporation, but retained in the stock book, and a receipt was indorsed thereon by the corporation for him, it was held that there was no de-livery. York v. Passaic Rolling-Mill Co., 30 Fed. 471.

It must be borne'in mind, however, that, ordinarily, delivery of a certificate is not necessary to make a subscriber a stockholder. Ante, § 378(b).

714 Jones v. Terre Haute & Richmond R. Co., 17 How. Pr. (N. Y.) 529, 531.

555; ante, § 378(f).

717 Heslin v. Eastern Bldg. & Loan Ass'n of Syracuse, 28 Misc.

Rep. (N. Y.) 376. In Heslin v. Eastern Bldg. & Loan Ass'n of Syracuse, supra, it was held that a provision in a certificate of stock that any action against the corporation should be brought in the county in which its principal office was located was binding.

One who purchases through a trust company, and takes a certificate to the effect that the shares are on deposit in trust, which, together with a deed of transfer thereof, are to be delivered on demand, cannot insist that 715 See post, § 592.

716 Burr v. Wilcox, 22 N. Y. 551,

McClure v. Central Trust Co., 28

App. Div. (N. Y.) 433. issued, are to be in such form and signed by such officers.718 Omission of the corporate seal from a certificate of stock, which is otherwise in proper form, and signed by the proper officers, does not render it invalid.719

#### § 425. Right to certificates, and remedies for refusal to issue the same.

While a certificate of stock is not necessary to render one a stockholder in a corporation, it is desirable to have one as evidence and for the purpose of transfer, etc., and every stockholder has a right to a proper certificate as soon as he has paid for his shares, unless there is some provision or agreement to the contrary. 720 As a rule, a corporation is also under a duty to issue a certificate, or a new certificate, to a transferee of shares, unless it has a lien on the shares, or for some other reason is not bound to recognize the transfer.721 In the absence of a provision or agreement to the contrary, a corporation is not bound to issue a certificate for stock until it is paid for in full, 722 although, as we have seen in the preceding paragraph, it may do so unless prohibited. But if the contract of a subscriber makes him a stockholder without payment, and, by the terms of the contract, the shares are not to be paid for until a fixed time in the future, or are to be paid for in in-

of a corporation authorize or re-Burns, 82 Tex. 50; Birmingham quire its certificates of stock to be Nat. Bank v. Roden, 97 Ala. 404; issued in a particular form, and Fletcher v. McGill, 110 Ind. 395; signed by particular officers, all and other cases cited in the notes certificates are properly issued in certificates are properly issued in following. such form and signed by such officers, to whomsoever they may be issued. No other or different form named. Titus v. President, etc., of the Great Western Turnpike Road, 61 N. Y. 237.

<sup>(</sup>N. S.; N. Y.) 170, 177.

<sup>720</sup> Appeal of Rowley, 115 Pa. St. 44 Ga. 597.

<sup>721</sup> Post, § 557 et seq.

<sup>722</sup> California Southern Hotel Co. is required in the case of certifi-v. Callender, 94 Cal. 120, 28 Am. cates issued to one of the officers St. Rep. 99; Baltimore City Pasamed. Titus v. President, etc., of amed. Titus v. President, etc., of the Great Western Turnpike Road, Md. 341, 2 Keener's Cas. 1033; Babcock v. Schuylkill & Lehigh Valley R. Co., 133 N. Y. 420; Fulgam v. Macon' & Brunswick R. Co., 720 Appeal of Baylor, 115 Bc. 54.

stallments as called for, payment is not necessary to entitle him to a certificate.

Remedies for refusal to issue certificates.—By the weight of authority, if a corporation wrongfully refuses to issue a proper certificate of stock when it has the power and is under an obligation to issue the same, mandamus will lie to compel it to do so.723 Or it may be compelled to do so by a suit in equity for specific performance of its express or implied contract. 724 Or, instead of suing to compel the issuance and delivery of a certificate, the party may maintain against the corporation an action of assumpsit on its express or implied contract, to recover damages for the breach thereof;725 or, if he has title to the

Co., 16 S. C. 524; State v. New Orleans Gas Light Co., 25 La. Ann.

less the petitioner's right is clear. a writ of mandamus should be denied where there is a controversy between the parties as to their legal rights under an agreement referred to in the certificate under which the petitioner claims the right to stock, and the nature of such agreement does not appear. Townes v. Nichols, 73 Me. 515.

As to the jurisdiction of the courts to compel a foreign corporation to issue certificates of stock,

see post, chapter xxvi.

In Ohio, where a statute provides that the writ of mandamus "must not be issued in a case where there is a plain and adequate remedy in the ordinary course of the law," it has been held that mandamus will not lie to compel a corporation to issue a certificate of stock, but that the remedy is either at law to recover damages for refusal to issue ciation, a person to whom one of the same, or in equity to compel the associates assigned his interthe officers of the corporation to est prior to incorporation may execute and deliver it. State v. maintain an action against the cor-St. Rep. 556.

723 State v. Cheraw & Chester R. v. Carpenter, 51 Ohio St. 83, 46 o., 16 S. C. 524; State v. New Am. St. Rep. 556; Appeal of Rowrleans Gas Light Co., 25 La. Ann. ley, 115 Pa. St. 150; Reading Iron Works' Estate, 149 Pa. St. 182; Since mandamus does not lie un-Manhattanville & St. N. Ave. Ry. Co., 140 N. Y. 183, affirming 1 Misc. Rep. 457; Blaisdell v. Bohr, 68 Ga. 56; Wells v. Green Bay & Mississippi Canal Co., 90 Wis. 442; Davenport v. Plano Implement Co., 70 Ill. App. 161.

725 Birmingham Nat. Bank v. Roden, 97 Ala. 404; Baltimore City Passenger Ry. Co. v. Sewell, 35 Md. 238, 6 Am. Rep. 402; Sargent v. Franklin Ins. Co., 8 Pick. (Mass.) 90, 19 Am. Dec. 306; Wyman v. American Powder Co., 8 Cush. (Mass.) 168; Salt River Canal Co. v. Hickey (Ariz.) 36 Pac.

Where the members of an unincorporated association become incorporated in pursuance of affagreement by which each of the associates is to have stock in proportion to his interest in the asso-Carpenter, 51 Ohio St. 83, 46 Am. poration in his own name for refusal to issue to him certificates 724 Williams v. Savage Mfg. Co., of stock for his interest. Balti-3 Md, Ch. 418; Birmingham Nat. more City Passenger Ry. Co., v. Bank v. Roden, 97 Ala. 404; State Sewell, 35 Md. 238, 6 Am. Rep. 402,

stock, he may treat the refusal to deliver a certificate as a conversion of the stock, and maintain an action of trover to recover damages. 726 The measure of damages in such actions is ordinarily the value of the stock at the time the certificate was demanded and refused, with interest, 727 deducting, of course, anything that may remain payable on the stock. 728

A subscriber for stock may, as against the corporation, rescind his contract of subscription, if the corporation wrongfully refuses to deliver a certificate, and sue to recover back what he has paid; and the rescission, if made before insolvency of the company, is good even as against creditors if the company afterwards becomes insolvent. 729 He cannot rescind for the first time, and recover what he has paid, after the corporation has become insolvent, and the rights of creditors have intervened.730

A stockholder's right of action against a corporation to compel it to deliver to him a certificate of stock, or to recover damages for its refusal to do so, does not accrue until the corporation denies his right thereto, and the statute of limitations, therefore, does not begin to run until then.\*

727 Sargent v. Franklin Ins. Co., 8 Pick. (Mass.) 90, 19 Am. Dec. 306; Wyman v. American Powder Co., 8 Cush. (Mass.) 168; Eastern R. Co. v. Benedict, 10 Gray (Mass.) 212; Jefferson v. Hale, 31 Ark. 286; State v. Carpenter, 51 Ohio St. 83, 46 Am. St. Rep. 556; Freon v. Carriage Co., 42 Ohio St. 38, 51 Am. Rep. 794; Salt River Canal Co. v. Hickey (Ariz.) 36 Pac. 171; Huntingdon & B. T. Railroad & Coal Co. v. English, 86 Pa. St. 247.

What has been said in a former section with reference to damages for the conversion of stock is ap- Canal Co., 90 Wis. 442.

726 State v. Carpenter, 51 Ohio plicable here, and many of the St. 83, 46 Am. St. Rep. 556. See cases there cited are in point. See ante, § 379.

728 Van Allen v. Illinois Central R. Co., 7 Bosw. (N. Y.) 515. Blaisdell v. Bohr, 68 Ga. 56.

729 Swazey v. Choate Mfg. Co., 48 N. H. 200; Potts v. Wallace, 32 Fed. 272.

A rescission and demand for repayment before commencement of the action is necessary. Swazey v. Choate Mfg. Co., supra.

730 See Pacific Nat. Bank v. Eaton, 141 U.S. 227, 2 Keener's Cas. English, 86 Pa. St. 247.

As to proof of value, see ante, \$ 234; Butler v. Eaton, 141 U. S. 240.

> \*Com. v. Springfield, M. & H. Turnpike Co., 10 Bush (Ky.) 254; Wells v. Green Bay & Mississippi

The rights and remedies of a transferee of shares are considered in a subsequent chapter.731

Exhaustion of power to issue stock.—When a corporation has already issued valid certificates of stock to the full amount authorized by its charter, and has no authority to increase the amount, no court can compel it to issue further certificates, for this would be to compel it to exceed its powers by making an overissue of stock;782 and in such a case, therefore, the only remedy of a person to whom it has expressly or impliedly contracted to issue stock is an action to recover damages. 733

#### § 426. Rights and remedies in case of loss of certificate of stock.

A corporation may issue, and in a proper case may be compelled to issue, a new certificate of stock in the place of an original certificate which has been stolen, destroyed, or otherwise lost by the owner. The issue of a new certificate in such a case is not an overissue of stock.735 Whether or not the corporation can require the owner of the lost certificate to give a bond to indemnify it against possible liability on the original certificate depends upon the circumstances.

As we shall hereafter see, if a corporation issues a certificate of stock, it thereby represents that the person named therein is the owner of the number of shares designated therein, and that he has a right to transfer the same, and it will be estopped to deny this representation as against a bona fide transferee, at least to such an extent as to entitle him to re-

<sup>731</sup> Post, § 602 et seq.

Cas. 874, 2 Smith's Cas. 1109, 2 ican Min. Co., 1 Nev. 423. Cum. Cas. 119; Smith v. North 734 See the cases cited in the American Min. Co., 1 Nev. 423; notes following.

issued some certificates to the 732 See ante, § 405 et seq. wrong persons gives the court no power to compel it to issue other certificates to the persons entitled, Haven R. Co., 13 N. Y. 599; New York & New Haven R. Co. v. Schuyler, 34 N. Y. 30, 1 Keeper's heap issued. York & New Haven R. Co. v. amount of the capital stock have Schuyler, 34 N. Y. 30, 1 Keener's been issued. Smith v. North Amer-

Kiner Kan Min. Co., 1 Nev. 423, hotes following.
Finley Shoe & Leather Co. v. 735 Kinnan v. Forty-Second Kurtz, 34 Mich. 89; Williams v. Street, Manhattanville & St. N. Savage Mfg. Co., 3 Md. Ch. 418.

The fact that a corporation has N. Y. 183.

cover damages. 786 It follows that if the owner of a certificate should transfer the same, and then, representing that it has been lost or stolen, induce or compel the corporation to issue to him a new certificate, and afterwards transfer it, the corporation would incur liability upon both certificates. It has accordingly been held that a corporation cannot be compelled to issue a new certificate in the place of one which is asserted to have been lost or stolen, unless a bond is given to indemnify it against liability to possible bona fide holders of the original certificate, at least without the clearest proof that it has in fact been lost or stolen, so that the corporation will not be liable to the holder.<sup>737</sup> The corporation, however, may be compelled to issue a new certificate if a bond of indemnity is given; and it has been held that it may be compelled to issue a new certificate without any indemnity, if there is clear proof that the original has been destroyed, or that it has been lost or stolen, not having an assignment thereon by the owner, or if the corporation is otherwise protected, for in such a case the corporation cannot incur any liability by reason of the original certificate. 738

In some jurisdictions, provision is made by statute for the issue of a new certificate in the place of one lost or stolen, upon

736 Post, § 428 et seq. 737 Galveston City Co. v. Sibley, 56 Tex. 269; Guilford v. Western

738 Guilford v. Western Union Tel. Co., 59 Minn. 332, 50 Am. St. Rep. 407; State v. New Orleans Gas Light Co., 25 La. Ann. 413 (where it was held that, as the stock was only transferable on the books of Minn. 332, 50 Am. St. Rep. 407. the company and surrender of the

A judgment against the plaintiff in an action to compel the issue of a new certificate without Union Tel. Co., 43 Minn. 434, 59 indemnity is not res judicata, so as Minn. 332, 50 Am. St. Rep. 407; to bar another action, where suffi-Butler v. Glen Cove Starch Mfg. cient time has elapsed since the Co., 18 Hun (N. Y.) 47. See, also, former judgment to make out sat-Chesapeake & Ohio Canal Co. v. isfactory proof of loss of the orig-Blair, 45 Md. 102; Societe Generale inal certificate. Guilford v. West-De Paris v. Walker, 11 App. Cas. ern Union Tel. Co., 59 Minn. 332, 50 Am. St. Rep. 407.

A mere custom of a corporation not to issue new certificates without a bond of indemnity is not binding on its stockholders. Guilford v. Western Union Tel. Co., 59

That the corporation may mark certificate, this was a sufficient the new certificate "duplicate" was protection); Hof v. Western German Bank, 6 Wkly. Law Bul. chine Mfg. Co., 43 Mo. App. 84 (Ohio) 665, 697. giving indemnity, or without indemnity, if the loss is clearly proved.<sup>739</sup> It has been held, however, that the remedy provided by such a statute is merely cumulative, and does prevent the owner of a lost certificate from resorting to any other appropriate remedy,—as, for example, a suit in equity to compel issue of a certificate.740

The rights and liabilities of purchasers of lost or stolen certificates are considered in another chapter.741

#### § 427. Cancellation of certificates.

If certificates of stock are issued illegally, or by an officer fraudulently or without authority, and the circumstances are such that they are either void or voidable, the corporation may cancel the same, or a suit in equity to cancel the same and enjoin their transfer may be brought by the corporation, or, in a proper case, by a stockholder.742

Guilford v. Western Union Tel. Co., 59 Minn. 332, 50 Am. St. Rep. 407; Laws N. Y. 1892, c. 688, §§ 50, 51.

Under a statute authorizing a court to compel a corporation to issue stock certificates in the place of certificates lost or destroyed, on proof that such certificates cannot be found by due diligence, a petitioner for such relief is not entitled thereto, where it appears that he himself has some of the certificates, and that others are in the possession of third persons, who refuse to surrender them. Biglin v. Friendship Ass'n, 46 Hun (N. Y.) 223.

In North Carolina the statute manner of reissuing certificates of stock where the original has been lost, requiring an indemnity bond, and permitting the corporation to corporations. Carolina R. Co., 125 N. C. 124.

739 See Laws Minn. 1893, c. 45; cedure in an action to compel issue of a new certificate, and as to the province of the court and jury therein.

> 740 Kinnan Forty-Second v. Street, Manhattanville & St. N. Ave. Ry. Co., 140 N. Y. 183, affirming 1 Misc. Rep. 457.

741 See post, § 597.

742 New York & New Haven R. Co. v. Schuyler, 34 N. Y. 30, 1 Keener's Cas. 874, 2 Smith's Cas. 1109, 2 Cum. Cas. 119; Wood v. Union Gospel Church Bldg. Ass'n, 63 Wis. 9; Bailey v. Champlain Mining & Prospecting Co., 77 Wis. 453; Perry v. Tuskaloosa Cotton Seed Oil Mill Co., 93 Ala. 364.

In an Alabama case it was held (Laws 1885, c. 265) regulating the that a demurrer to a bill for the cancellation of certificates of stock was improperly sustained, where it showed that the president of the corporation, for the purpose of retain the new certificate for five gaining control, convened a meetyears as a further safeguard, is a ing of the directors, and presented general provision applicable to all his account for work done for the Hendon v. North corporation, and the accounts of third persons for materials fur-See this case, also, as to the pro- nished under a contract made by

If the corporation wrongfully cancels a certificate of stock, and refuses to recognize the owner as a stockholder, it is guilty of a conversion of the stock, and liable in an action to recover damages therefor.743 Or it may be compelled to issue a new certificate.744

If a certificate is surrendered to a corporation through a mistake of fact, and canceled, a court of equity has power to compel the corporation to reissue it, or to issue a new certificate, if the authorized amount of capital stock will not be thereby exceeded 745

- IX. RIGHTS AND LIABILITIES ARISING OUT OF ISSUE OF FICTITIOUS CER-TIFICATES OF STOCK.
- § 428. In general.—An overissue of stock is void, and the certificates thereof cannot make the holders stockholders. corporation is liable in damages to bona fide purchasers or pledgees of fictitious certificates of stock, if they were issued by an officer or agent under authority from the corporation or its managing officers, or by an officer or agent clothed with apparent authority, although his act may have been in fact unauthorized, and fraudulent, or even a forgery; or if their issue, and the consequent injury, were the result of negligence on the part of the corporation or its managing officers.746

#### § 429. Overissue of stock is void.

As we have seen in a former section, a corporation is abso-

him; that the certificates sought to be canceled were thereupon issued to him and to such third persons in payment of these accounts, without any auditing or investigaaccounts; that such third persons agreed with the president to hold their shares for his benefit; and that there were present at the meeting, besides the president, only two other directors, both of the marine Dry-Dock & Snipyard Co., As to proof of cancellation, see Topeka Mfg. Co. v. Hale, 39 Kan. 23.

744 Ante, § 425.

745 Williams v. Savage Mfg. Co., W. Hale, 39 Kan. 24. whom owned little stock, and were 3 Md. Ch. 418. his tools. Perry v. Tuskaloosa Cotton Seed Oil Mill Co., 93 Ala. between the transferrer and trans-364.

As to cancellation for breach of contract by the holder, see Pendleton Mfg. Co. v. Mahanna (Ore.) 18 Pac. 563.

743 Factors' & Traders' Ins. Co. v. tion as to the correctness of the Marine Dry-Dock & Shipyard Co.,

746 The rights and labilities as feree, or vendor and vendee, of

lutely without the power to increase its capital stock beyond the amount fixed by its charter or the general law under which it was organized, or by its articles of association or incorporation, in pursuance thereof, unless such power has been conferred upon it by the legislature. It necessarily follows that certificates of stock issued by a corporation, which represent an overissue of stock, are absolutely void, and cannot give the holders thereof the status of stockholders.747 As we shall see in the following sections, however, it does not follow that the issue of fictitious and void certificates can impose no liability upon the corporation.

# § 430. Liability of corporation in damages.

It is a well-settled principle that a certificate of stock issued by a corporation having the power under its charter to issue certificates in the form in which the certificate is issued is a continuing affirmation or representation of the ownership of the amount of stock therein specified by the person named therein, or his assignee, and of his right to transfer the same, and that purchasers or pledgees of the certificate, or the stock represented by it, have a right to rely on such affirmation, without inquiry as to the validity of the certificate, unless they have actual notice of its invalidity, or the circumstances are such as to create suspicion, and put a reasonably prudent man upon inquiry.748 is also a well-settled principle, as we have seen, that a corporation is liable to the same extent and under the same circumstances as a natural person, for every fraud which it commits, and for negligence and other wrongs, however foreign to its nature or beyond its granted powers the wrongful transaction or

spurious certificates, are considered in a subsequent chapter. See post, §§ 613, 625.

748 Holbrook v. New Jersey Zinc Co., 57 N. Y. 616, 2 Cum. Cas. 152; Appeal of Kisterbock, 127 Pa. St. eu in a subsequent chapter. See Co., 57 N. Y. 616, 2 Cum. Cas. 152; post, §§ 613, 625.

Appeal of Kisterbock, 127 Pa. St. 747 New York & New Haven R. 601, 14 Am. St. Rep. 868; Joslyn v. Co. v. Schuyler, 34 N. Y. 30, 1

Keener's Cas. 874, 2 Smith's Cas. 183, 2 Keener's Cas. 1073, 2 Cum. 1109, 2 Cum. Cas. 119. And see Cas. 177; and other cases in note ante, § 407(g), and cases there 751, infra.

act may be.749 It follows from these principles that if a corporation itself, or an officer or agent for whose act it is responsible.750 fraudulently, or even by mistake and without any actual fraudulent intent, issues certificates of stock which are fictitious because they are in excess of its authorized capital stock. or otherwise unauthorized, it is liable in damages to bona fide purchasers or pledgees of such certificates who are deceived and injured by relying upon their genuineness. And in an action to recover damages, upon refusal of the corporation to recognize the validity of such a certificate, the corporation is estopped to set up as a defense that it had no power to create the stock or issue the certificate. 751

1109, 2 Cum. Cas. 119. See ante, § 236 et seq.

750 Post, § 431.

751 Shaw v. Port Philip & Colonial Gold Min. Co., 13 Q. B. Div. 103; New York & New Haven R. Co. v. Schuyler, 34 N. Y. 30, 1 Keener's Cas. 874, 2 Smith's Cas. 1109, 2 Cum. Cas. 119; Holbrook v. New Jersey Zinc Co., 57 N. Y. 616, 2 Cum. Cas. 162; Titus v. President, etc., of the Great Western Turnpike Road, 5 Lans. (N. Y.) 250, 61 N. Y. 237; Fifth Avenue Bank v. Forty-Second Street & Grand Street Ferry R. Co., 137 N. Y. 231, 33 Am. St. Rep. 712, 2 Keener's Cas. 915, 2 Cum. Cas. 149; Jarvis v. Manhattan Beach Co., 53 Hun, 362, 148 N. Y. 652, 51 Am. St. Rep. 727; Bridgeport Bank v. New York & New Haven R. Co., 30 Conn. 231; Tome v. Parkersburg Branch R. Co., 39 Conn. R. Co., 39 Md. 36, 17 Am. Rep. 540; Moores v. Citizens' Nat. Bank of Piqua, 111 U. S. 156, 2 Cum. Cas. 144; Manhattan Beach Co. v. Harrand 27 Fed. 424; Cincipneti New ned, 27 Fed. 484; Cincinnati, New Orleans & T. P. Ry. Co. v. Citizens' Nat. Bank, 56 Ohio St. 351; Appeal of Kisterbock, 127 Pa. St. 601, 14 was held that he could recover his Am. St. Rep. 868; Swain v. West damages from the corporation. Philadelphia Passenger Ry. Co., Jarvis v. Manhattan Beach Co., 53

749 New York & New Haven R. cited 127 Pa. St. 616, 14 Am. St. Co. v. Schuyler, 34 N. Y. 30, 1 Rep. 871; Mt. Holly Paper Co.'s Keener's Cas. 874, 2 Smith's Cas. Appeal, 99 Pa. St. 513; People's Appeal, 99 Pa. St. 513; People's Bank v. Kurtz, 99 Pa. St. 344, 44 Am. Rep. 112; Bank of Kentucky v. Schuylkill Bank, 1 Pars. Sel. Cas. (Pa.) 180; Willis v. Philadelphia & Darby R. Co., 6 W. N. C. (Pa.) 461; Allen v. South Boston R. Co., 150 Mass. 200, 15 Am. St. Rep. 185, 2 Keener's Cas. 909; Farrington v. South Boston R. Co., 150 Mass. 406, 15 Am. St. Rep. 222; Joslyn v. St. Paul Distilling Co., 44 Minn. 183, 2 Keener's Cas. 1073, 2 Cum. Cas. 177.

Where the transfer clerk of a corporation fraudulently procured from the officers of the corporation a properly signed certificate of stock in the name of a fictitious indorsed the fictitious name thereon, and caused it to be registered on the transfer book, and caused a broker to sell the certificate for the fictitious person, after he inquired at the office of the corporation, and was informed that the stock was duly registered, and the broker paid the proceeds over to the transfer clerk, and was afterwards compelled to take back the certificate from the purchaser, and refund the purchase money, it

This principle also applies when a corporation, or an officer or agent for whose act it is responsible, recognizes as valid a forged or unauthorized transfer of stock, and issues a new certificate to the transferee, and the new certificate comes into the hands of a bona fide purchaser for value. 752 And if a corporation transfers shares of stock on its books, and issues new certificates, leaving the original certificates outstanding, it will be liable to bona fide purchasers or pledgees of the stock who purchase or lend money on the same in reliance upon the original certificates.753 This is true, even when the corporation, in making the transfer and issuing the new certificates, acted in obedience to a decree of a court, for the decree cannot affect the rights of persons who were not parties to the suit.754

The rights and liabilities as between the transferrer and transferee of fictitious or overissued certificates of stock are considered in another place.755

#### § 431. Authority of officer or agent issuing certificate.

Difficult questions have arisen in determining the liability of a corporation by reason of false certificates of stock, where the corporation has sought to escape liability on the ground that the certificates were issued by officers or agents without authority. The liability in such a case is to be determined by applying the

N. Y. 652, 51 Am. St. Rep. 727.

in cases specifically referred to

A loan association whose secretary customarily issues, in lieu of certificates, statements under the corporate seal, and attested by him. that persons therein named appear reliance thereon. Richardson v. Keener's Cas. 1076, 2 Cum. Cas. Delaware Loan Ass'n, 9 Houst. 179. And see post, § 607. (Del.) 354.

752 Simm v. Anglo-American Tel- ceding. egraph Co., 5 Q. B. Div. 188, 2

Hun (N. Y.) 362, 75 Hun, 100, 148 Keener's Cas. 1148, 2 Cum. Cas. 165; Mandlebaum v. North Amer-And see many other illustrations ican Min. Co., 4 Mich. 465, 2 Cum. Cas. 159; Machinists' Nat. Bank v. Field, 126 Mass. 345, 1 Keener's Cas. 894, 2 Cum, Cas. 175. And see post, § 599.

753 Holbrook v. New Jersey Zinc Co., 57 N. Y. 616, 2 Cum. Cas. 152; Joslyn v. St. Paul Distilling Co., 44 as stockholders on its books, is Minn. 183, 2 Keener's Cas. 1073, 2 bound by such a statement to one Cum. Cas. 177; Bean v. American who in good faith makes a loan in Loan & Trust Co., 122 N. Y. 622, 2

755 Post, §§ 613, 625.

general principles of the law of agency. There can be no question as to the liability of the corporation when the false certificates are issued by or in pursuance of the vote or consent of a majority of the stockholders, for the issue is then the direct act of the corporation. Nor can there be any doubt as to its liability where they are issued by or in pursuance of a vote or direction of the board of directors expressly or impliedly vested with the general authority to issue or authorize the issue of certificates of stock, or by other officers in whom such authority is vested. The liability is not so clear, however, when the certificates are issued by subordinate officers or agents without authority in fact from the stockholders or board of directors.

It is a general principle that a corporation, like a natural person, is liable for acts, including fraud and other wrongs, done by its officers or agents in the course of their employment, and within either the real or the apparent scope of the powers delegated to them. If a particular act is within the apparent scope of the authority conferred upon an officer or agent of a corporation, the corporation is liable therefor, although the act may have been in fact unauthorized, or even contrary to instruc-It follows that a corporation is liable for the fraudulent or wrongful issue of false certificates of stock by an officer or agent whom it had clothed with general or apparent authority to issue certificates in the form in which the false certificates were issued, although the issue of the false certificates may have been unauthorized, and although they may have been issued by the officer or agent for his own purposes, and not for the purposes of the corporation. The ground of liability, said the Maryland court, "is not that the principal has been benefitted by the act of the agent, but that an innocent third person has

<sup>756</sup> See post, chapter xxiv.

Bank v. New York & New Haven R. Co., 30 Conn. 231; Tome v. Par-Co. v. Schuyler, 34 N. Y. 30, 1 kersburg Branch R. Co., 39 Md. 36, Keener's Cas. 874, 2 Smith's Cas. 17 Am. Rep. 540; and cases cited 1109, 2 Cum. Cas. 119; Bridgeport in the notes following.

been damaged by confiding in the agent, who was accredited by the principal, as worthy of trust, in that particular business."758

On the other hand, however, the corporation is not liable if the issue of the false certificates was not within either the actual or the apparent scope of the officer's or agent's authority, unless it has been guilty of negligence in the premises.759

#### § 432. Forged certificates.

Whether or not a corporation is liable to a bona fide purchaser of a false certificate of stock, where the officer or agent issuing the same forged the necessary signatures of the other officers, depends upon the circumstances. The proper rule in such a case is that the corporation is liable if the ability of the guilty officer to commit the forgery and fraudulently issue the certificate, and the failure of the purchaser or pledgee to discover the forgery, were not due to any want of ordinary care on his part, or if the forgery was committed and the certificate issued by an officer intrusted with the duty of finally countersigning and issuing the certificate, but not otherwise. This statement of the law is not laid down in so many words in any of the cases, but it is clearly deducible from the decisions, as will be seen from the following cases.

R. Co., 39 Md. 36, 17 Am. Rep. 540. 759 President, etc., of the Mechan-Tos President, etc., of the Mechanics' Bank v. New York & New Haven R. Co., 13 N. Y. 599; Manhattan Life Ins. Co. v. Forty-Second Street & Grand Street Ferry R. Co., 64 Hun (N. Y.) 635, 139 N. Y. 146; Knox v. Eden Musee American Co., 148 N. Y. 441, 51 Am. St. Rep. 700, 2 Keener's Cas. 1121, 2 Smith's Cas. 1100. Moores v. Citi-Smith's Cas. 1100; Moores v. Citiens' Nat. Bank of Piqua, 111 U. S. 156, 2 Cum. Cas. 144.

758 Tome v. Parkersburg Branch to a bona fide purchaser or pledgee of certificates of stock constituting a fraudulent overissue, where they were issued by the president of the

corporation, who was intrusted merely with the transfer of stock. In a Pennsylvania case, the president of a railroad company, by fraudulently representing to his aunt that a loan of her shares of stock in the company was needed by the company, induced her to part with them, and then pledged 156, 2 Cum. Cas. 144.

See, also, post, chapter xxiv., wards he conspired with other on this question is further cers of the company to procure a fraudulent overissue of stock, and them for his own debt. After-In President, etc., of the Mechan- transferred some of it to his aunt ics' Bank v. New York & New Ha- in lieu of her shares. It was held ven R. Co., 13 N. Y. 599, it was held that she could not hold the comthat a corporation was not liable pany liable, as he acted as her

In an English case, a corporation was held responsible for the act of its secretary in fraudulently issuing a false certificate to a transferee, upon which he forged the necessary signature of a director, where it was part of the authorized and regular duty of the secretary to receive and examine transfers and certificates of shares, to have transfers registered, to procure the preparation, execution, and signature of certificates, with all requisite and prescribed formalities, and thereupon to issue them to the persons entitled to receive them. 760

In a Maryland case, where the treasurer of a corporation was charged with the duty, under the by-laws, of keeping the books relating to the ownership and transfer of stock, preparing and countersigning all certificates of stock, receiving and entering transfers, affixing the corporate seal to certificates properly issued by the company, and signed by the president, and issuing certificates, it was held that the corporation was liable for his act in fraudulently issuing a false certificate countersigned by himself, and sealed with the corporate seal, whether the signature of the president thereon was forged or not.761

In a Massachusetts case, where the by-laws of a corporation required certificates of stock to be under the seal of the company, and signed by the president and treasurer, but gave the president nothing whatever to do with respect to the issuing of certificates except signing the same, it was held that the corporation was not liable at all upon certificates fraudulently issued by the president for his own benefit, and upon which he signed his own name, forged the name of the treasurer, and impressed the corporate seal, unless the corporation was chargeable with negligence; and that the fact that the corporation allowed the president to continue in office, and to have access to its certificate book and seal after misconduct on his part consisting merely in violating an agreement to pledge certain stock to his associates

agent, and not as the agent of the St. 425.

agent, and not as the agent of the company. Wright's Appeal, 99 Pa. nial Gold Min. Co., 13 Q. B. Div. 103. 761 Tome v. Parkersburg Branch R. Co., 39 Md. 36, 17 Am. Rep. 540.

in the corporation was not sufficient to render it liable on the ground of negligence.762

In a New York case, a corporation was held liable for the act of its secretary and treasurer in fraudulently issuing a false certificate countersigned by him as secretary, and under the seal of the corporation, and upon which he had forged the necessary signature of the president, and signed his own name as treasurer, where it appeared that he was the transfer agent of the corporation, and had authority generally to countersign certificates of stock, when signed by the president and treasurer, and to seal them with the corporate seal. The court held that his countersigning and sealing constituted an affirmation on the part of the corporation that all conditions precedent upon which the right to issue the certificate depended had been duly observed, and that the stock was lawfully issued. 763

In another New York case it appeared that in 1881 the then president of a corporation signed certificates of stock in blank, and left them with the other officers of the corporation to be used, if necessary, in his absence. In 1888 a person who was transfer agent and secretary in 1881, but had since become the president, filled up and antedated one of these certificates to himself as stockholder, forging the name of the person who was treasurer of the corporation in 1881, and signing his own name as transfer agent, which he was in 1881, but had since ceased to be, and pledged the certificate as collateral security for a loan made to him personally. Under these circumstances, it was held that the corporation was not liable on the forged certificate, as the forger, as president, had no authority, actual or apparent, to issue a certificate, as his authority as transfer agent had ceased to exist, so that he was not empowered to sign as such, and antedate it as of the time when he held that office; and also

<sup>762</sup> Hill v. Jewett Publishing Co., Rep. 712, 2 Keener's Cas. 915, 2 154 Mass. 172, 26 Am. St. Rep. 230. Cum. Cas. 149. See, also, Mutual 763 Fifth Avenue Bank v. Forty-Life Ins. Co. v. Forty-Second Street Second Street & Grand Street Ferry R. Co., 74 ry R. Co., 137 N. Y. 231, 33 Am. St. Hun (N. Y.) 505.

because, when he borrowed the money and issued the certificate, he was not acting in the company's business, and the company was not responsible for any representations made by him as to the genuineness of the certificate. 764

# § 433. Certificates signed in blank.

If a corporation or its managing officers intrust the officer or agent charged with the duty of registering transfers and issuing certificates with certificates of stock signed in blank by the officers by whom the by-laws require certificates to be signed, it will be liable if a certificate is fraudulently filled up and issued by such officer or agent, and comes into the hands of a bona fide purchaser or pledgee, not only on the ground of apparent authority, but also on the ground of negligence. Intrusting the officer or agent charged with the duty of issuing certificates with certificates signed in blank removes the safeguards against the fraudulent issue of false certificates intended by the by-laws,—the necessity for the approval and signature of the specified officers,—and is clearly negligence.

In a late Massachusetts case, the treasurer of a corporation authorized a broker to sell a number of shares for him, and the broker sold shares to the plaintiff, giving him power of attorney, in blank, authorizing the transfer of the shares to him. The plaintiff presented the power of attorney to the treasurer, who filled in the purchaser's name and his own name as attorney, and thereupon issued to the plaintiff the number of shares called for, entering in the transfer book a transfer of the shares from himself, as treasurer, to the broker, and a transfer from the broker to the plaintiff. The shares so issued were a fraudulent overissue. It appeared, however, that the president of the corporation was in the habit of leaving blank certificates signed by him with the treasurer, and the latter, by signing and issuing these certificates and falsifying the records of the corporation,

764 Manhattan Life Ins. Co. v. Forty-Second Street & Grand Street Ferry R. Co., 139 N. Y. 146. was enabled to make the overissue. Under these circumstances, it was held that, as the negligence of the officers of the corporation made the fraudulent overissue possible, the corporation was liable to the plaintiff for his damages.<sup>765</sup>

### § 434. Stolen certificates.

It is a general principle that if a stock certificate is lost by the owner without negligence, or stolen, no title or right is acquired as against the owner either by the finder or thief or by a bona fide purchaser, and this principle applies where certificates are stolen from a corporation by one of its officers or employes, and fraudulently issued by him to a bona fide purchaser or pledgee. In such a case, if the officer or agent has no authority to issue certificates, and no negligence is imputable to the corporation, it is not liable to a bona fide purchaser of the certificates; and the fact that the officer or agent was intrusted with the custody of the certificates does not show negligence if the corporation had no reason to believe him to be untrustworthy. New York case, the lower court held a corporation liable for injury caused by the act of its manager in fraudulently issuing surrendered but uncanceled certificates of stock, where the certificates, having upon them assignments in blank, had been surrendered to the corporation on the issue of new certificates in their stead, and were placed uncanceled in the safe of the corporation, to which the manager had access, with directions to him to cancel the same, as required by the by-laws, and the manager, instead of cancelling them, took them from the safe and pledged them as collateral for a loan from the plaintiff, who took them in good faith, and where it appeared that the manager had been in the employ of the corporation for several years, and that it had perfect confidence in his integrity. The court of appeals reversed the judgment, and held that the corporation The judgment could not be sustained, it was was not liable.

<sup>765</sup> Allen v. South Boston R. Co., cinnati, New Orleans & T. P. Ry. 150 Mass. 200, 15 Am. St. Rep. 185, Co. v. Citizens' Nat. Bank, 56 Ohio 2 Keener's Cas. 909. See, also, Cin-St. 351.

held, on the ground that the certificates were negotiable instruments, for the negotiability of certificates of stock does not extend so far as to prevent the owner of certificates which have been lost or stolen without his negligence from claiming them even from a bona fide purchaser. Nor could the judgment be sustained on the ground of agency, for an officer of a corporation in whose custody surrendered certificates of stock are placed, with directions to cancel them, has no implied authority to reissue them. Nor could it be sustained on the ground of negligence, for an employer is not to be deemed negligent merely because he intrusts his property to the custody of his agent, and does not anticipate or provide against the possibility of criminal acts on the part of the agent, where he has no reason to doubt the latter's integrity. It was further held that negligence was not imputable to the corporation in this case merely because of the violation in a single instance of a by-law by issuing a new certificate of stock without first cancelling the old certificate, which was surrendered, nor because the officers of the corporation omitted for the period of three weeks to ascertain whether a surrendered certificate of stock had been canceled by the manager in accordance with his duty, since the consequence for which a negligent person is answerable "must be the natural consequence of the alleged negligent act or one which might reasonably have been anticipated."766

### § 435. Persons who are entitled to relief.

The right of persons to hold a corporation liable because of the issue of fictitious certificates of stock is not based upon the stock which the certificates purport to represent, for, as we have seen, there is no such stock, but it is based upon the ground that bona fide purchasers or pledgees who have parted with heir money in reliance upon the certificate being valid are entitled to be indemnified. "The right to relief," said the supreme court of Pennsylvania in a late case, "depends upon the equity

<sup>&</sup>lt;sup>766</sup> Knox v. Eden Musee Ameri- Rep. 700, 2 Smith's Cas. 1100, 2 cain Co., 148 N. Y. 441, 51 Am. St. Keener's Cas. 1121.

of the person claiming it. If he has expended money upon the faith of the official certificates of the officers of the company, he has a right to be indemnified, to the extent of his expenditures, against loss from false certificates, but only because of the fact of his expenditures. The false certificates are no certificates in legal contemplation, and give no rights of their own force. But the act of the officers in issuing them, having been accepted and acted upon by another, the company cannot be heard to deny the truth of the fact represented. It is simply the application of the principle that, 'if you make a representation with the intention that it shall be acted upon by another, and he does so, you are estopped from denying the truth of what you represent to be the fact."767

It follows from this that liability upon the part of the corporation exists only in favor of persons who have paid or advanced money on the faith of the fictitious certificates. The company is not liable to one who has taken such a certificate merely in payment of or as security for an antecedent debt, at least if no damages have been sustained by releasing or surrendering other security, for such a person has expended nothing on the faith of the certificate. 769 Nor is it liable to a purchaser of the stock in reliance on the certificate, where he has not paid for it. 770

One who acquires fraudulently issued certificates of stock in payment of margins in the purchase of cotton for future delivery is not in a position to assert title thereto as against the corporation.771

In all cases, the person seeking relief against the corporation

767 Judge Green in Appeal of Kisterbock, 127 Pa. St. 601, 14 Am. an overissue, issued by the presists. Rep. 868, 871, citing Freeman dent of a corporation on the auv. Cooke, 2 Exch. 654, and In re Bahia & San Francisco Ry. Co., L. appointed by the directors out of R. 3 Q. B. 585, 2 Smith's Cas. 1092.

768 Appeal of Kisterbock, 127 Pa. St. 601, 14 Am. St. Rep. 868.

769 Appeal of Kisterbock, 127 Pa. St. 601, 14 Am. St. Rep. 868.

N. Y. 83.

thority of an executive committee appointed by the directors out of their number, but without authority from or ratification by the directors, confer no rights on one who is not a bona fide holder for value. Ryder v. Bushwick R. Co., supra.

t. 601, 14 Am. St. Rep. 868. 771 Miller v. Houston City Street 770 Ryder v. Bushwick R. Co., 134 Ry. Co., 30 U. S. App. 402, 69 Fed.

must be in the position of a bona fide purchaser or pledgee. The corporation, therefore, is not liable to one who has purchased the certificate or loaned money upon it with actual knowledge of its invalidity, or with notice of facts which were sufficient to put a reasonably prudent man upon an inquiry or investigation which, if followed up with reasonable diligence, would have disclosed its invalidity.772

When a person, in taking a certificate of stock from an officer of a corporation, whose duty it is to issue certificates, is dealing with the officer personally, as where the officer is selling the stock or pledging it for money loaned to himself, this fact is sufficient to put the person taking the certificate on inquiry, and if he relies on the representations of the officer without making further and independent inquiry, he is guilty of such negligence as to exclude him from the position of a bona fide purchaser or pledgee.<sup>773</sup>

Where an officer of a corporation issues a false certificate of stock as security for money loaned to him personally, representing that he owns such an amount of stock, and that the stock has been transferred to the lender on the books of the corporation, as required by the by-laws, and stated on the certificate, the representations are made by him personally, and not as the agent of the corporation, and the corporation is not responsible therefor to the lender.774

772 Moores v. Citizens' Nat. Bank of Piqua, 111 U.S. 156, 2 Cum. Cas. 144; Farrington v. South Boston R. Co., 150 Mass., 406, 15 Am. St. Rep. 221; Ryder v. Bushwick R. Co., 134 N. Y. 83; Hayden v. Charter Oak Driving Park, 63 Conn. 142.

773 Moores v. Citizens' Nat. Bank of Piqua, 111 U.S. 156, 2 Cum. Cas. 144; Farrington v. South Boston R. Co., 150 Mass. 406, 15 Am. St. Rep. 222; Cincinnati, New Orleans chapter xxiv.

774 Moores v. Citizens' Nat. Bank of Piqua, 111 U.S. 156, 2 Cum, Cas. 144; Farrington v. South Boston R. Co., 150 Mass. 406, 15 Am. St. Rep. 222.

In a late Ohio case, however, it was held that, where certificates of stock are required to be issued by the president and the secretary under the seal of the company, and no other mode is provided or can be used, and neither the secretary & T. P. Ry. Co. v. Third Nat. Bank nor the president is prohibited of Urbana, 1 Ohio Cir. Ct. Rep. 199. from holding stock, and both, with See, also, Wilson v. Metropolitan its knowledge, do in fact hold stock, Elevated Ry. Co., 120 N. Y. 145, the fact that a certificate is issued 17 Am. St. Rep. 625. And see post, in favor of the secretary is not of itself sufficient to put a party upon itself sufficient to put a party upon

In a case in the supreme court of the United States, the cashier of a bank borrowed money for his own use, representing that he was the owner of a certain amount of stock in the bank, which he offered as collateral, and that it had been transferred to the lender on the books of the bank, and issued directly to the lender as collateral a false certificate of stock by filling out a certificate which had been signed in blank by the president, and left with him for proper issue when needed, and the lender took the certificate on his representations, and without inquiring at the bank, although it recited on the face of it that no certificate of the stock could be lawfully issued without the surrender of a former certificate, and a transfer thereof on the books of the bank, and it was held that the lender was not in the position of a bona fide purchaser and could not hold the bank liable.<sup>775</sup>

There was a like decision in a comparatively late Massachusetts case, where the treasurer of a corporation issued a false and fraudulent certificate as collateral for a loan made to him personally. It was further held in this case that the lender acquired no additional right or equity from the fact that the certificate fraudulently issued to him was afterwards surrendered by him, and a new one issued therefor by the same officer.<sup>776</sup>

inquiry as to whether the secretary is rightfully the owner of it. Cincinnati, New Orleans & T. P. Ry. Co. v. Citizens' Nat. Bank, 56 Ohio St. 351.

775 Moores v. Citizens' Nat. Bank of Piqua, 111 U.S. 156, 2 Cum. Cas. 144. Mr. Justice Gray said in delivering the opinion of the court: "The very form of the certificate was such as to put her (the lender) upon her guard. She was not applying to the bank to take stock, as an original subscriber or otherwise; but she was bargaining with Robert B. Moores (the cashier) for stock which she supposed him to hold as his own. She knew that she had not held or surrendered any certificate, and she never asked to see his certificate or a transfer thereof to her; and he in fact made no surrender to the bank or transfer on its books. She relied

on his personal representation, as the party with whom she was dealing, that he had such stock; and she trusted him as her agent to see the proper transfer made on the books of the bank. Having distinct notice that the surrender and transfer of a former certificate were prerequisites to the lawful issue of a new one, and having accepted a certificate that she owned stock, without taking any steps to assure herself that the legal prerequisites to the validity of her certificate, which were to be fulfilled by the former owner and not by the bank, had been complied with, she does not, as against the bank, stand in the position of one who receives a certificate of stock from the proper officers without notice of any facts impairing its validity."

776 Farrington v. South Boston

In the cases above referred to, in which pledgees of false certificates of stock fraudulently issued by an officer of the corporation were held guilty of negligence in not ascertaining whether former certificates had been surrendered, and a transfer made on the books of the corporation, the necessity for which appeared on the face of the false certificates, the pledgees were dealing with the officer who issued the false certificates, and lending the money to him personally, and this fact made it their duty to inquire. A pledgee or purchaser of a certificate regular on its face, who is not dealing with the officer issuing it personally, owes no positive duty to the corporation to see to it that the seller or pledgor surrenders the old certificate, and makes an assignment on the books of the corporation, and he is not guilty of negligence merely in failing to do so. It is the duty of the corporation which requires these things to be done to see to it that they are done before a new certificate is issued to the purchaser,777

Where a person to whom an application for a loan is made, and to whom a certificate of stock is offered as collateral security. applies at the office of the corporation to the person in charge thereof, and who is its secretary and treasurer, and inquires whether the certificate is genuine, and receives an answer in the affirmative, and then makes the loan and takes the certificate as collateral, he is entitled to protection as a bona fide holder, and he does not lose his right to be so treated by selling the stock, and applying the proceeds to the payment of the loan, and afterwards, upon discovering that the certificate has been forged, taking an assignment thereof from the purchasers, and repaying them the amount paid by them at the sale.<sup>778</sup>

When a forged or unauthorized transfer of a certificate of stock is presented to the corporation for transfer on its books

R. Co., 150 Mass. 406, 15 Am. St. Ry. Co. v. Citizens' Nat. Bank, 56 Rep. 222. Ohio St. 351. Rep. 222.

<sup>777</sup> Allen v. South Boston R. Co., 778 Fifth Avenue Bank v. Forty-150 Mass. 200, 15 Am. St. Rep. 185; Second Street & Grand Street Ferry 778 Fifth Avenue Bank v. Forty-Farrington v. South Boston R. Co., R. Co., 137 N. Y. 231, 33 Am. St. 150 Mass. 406, 15 Am. St. Rep. 222; Rep. 712, 2 Keener's Cas. 915, 2 Cincinnati, New Orleans & T. P. Cum. Cas. 149.

and the issue of a new certificate, and the corporation recognizes the transfer and issues a new certificate to the transferee, it is not estopped to deny the validity of the new certificate as against him, for he has parted with his money in reliance, not on such certificate, but on the forged or unauthorized transfer, for which the corporation is not responsible. He is not in any way injured, therefore, by the act of the corporation in recognizing the transfer and issuing the new certificate.<sup>779</sup>

### § 436. Remedies of the corporation.

If the officers of a corporation fraudulently or wrongfully issue fictitious or illegal certificates of stock, the corporation, or, if it refuses to sue, a stockholder on behalf of himself and the other stockholders, may maintain a suit in equity to cancel the certificates, and to enjoin their transfer, or the voting thereon by the holders, or the payment of dividends thereon. And in such suit the court will determine and enforce any liability which the law may impose upon the corporation in favor of persons who have become bona fide purchasers or pledgees of the certificates.

An officer or agent who issues false certificates of stock is liable to the corporation for any damages sustained by it, and the corporation may maintain an action against him to recover the same. If he has received the proceeds of the certificate so issued by him, the corporation may waive the tort, and maintain an action of assumpsit for money had and received, and he cannot defeat the action by setting up as a defense the illegality in the issue of the stock.

779 Simm v. Anglo-American Telegraph Co., 5 Q. B. Div. 188, 2 Keener's Cas. 1148, 2 Cum. Cas. 165.

er's Cas. 1148, 2 Cum. Cas. 165.

780 New York & New Haven R.
Co. v. Schuyler, 17 N. Y. 592, 34
N. Y. 30, 1 Keener's Cas. 874, 2
Smith's Cas. 1109, 2 Cum. Cas. 119;
Hutton v. Joseph Bancroft & Sons
Co., 83 Fed. 17; Wood v. Union
Gospel Church Bldg. Ass'n, 63 Wis.
9; Davis v. San Antonio & Gulf
Vt. 39.

Shore Ry. Co. (Tex. Civ. App.) 44 S. W. 1012.

781 New York & New Haven R.
 Co. v. Schuyler, 34 N. Y. 30, 1
 Keener's Cas. 874, 2 Smith's Cas.
 1109, 2 Cum. Cas. 119.

<sup>782</sup> Brooklyn Crosstown R. Co. v. Strong, 75 N. Y. 591.

<sup>783</sup> Rutland R. Co. v. Haven, 62 Vt. 39.

As we have seen, if a corporation in good faith recognizes a forged or unauthorized transfer of stock, and issues a new certificate to the transferee, it is not estopped, as against him, to deny the validity of the transfer and the new certificate, for he has acted in reliance on the forged or unauthorized transfer, and not on the corporation's recognition thereof, nor on the new In such a case, therefore, as against him, the certificate.784 corporation may maintain a suit in equity to cancel the certificate before it reaches the hands of a bona fide purchaser; 785 or, if the corporation has been held liable thereon to a bona fide purchaser, it may maintain an action against the transferee for damages for inducing it to recognize the transfer and issue the certificate. 786

784 Ante, § 435. 785 See Simm v. Anglo-American Telegraph Co., 5 Q. B. Div. 188, 2 Eden, 299.
Keener's Cas. 1148, 2 Cum. Cas.
165; Hildyard v. South-Sea Co., 2
P. Wms. 76; Boston & Albany R.
v. Blackwee

Co. v. Richardson, 135 Mass. 473. Compare Ashby v. Blackwell, 2

786 Boston & Albany Railroad Co.

### CHAPTER XXI.

# SUBSCRIPTIONS TO CAPITAL STOCK AND OTHER AGREEMENTS TO TAKE STOCK.

- NATURE AND FORMATION OF CONTRACTS OF SUBSCRIPTION, AND OTHER AGREEMENTS.
  - § 437. In general.
    - 438. Subscriptions and other agreements defined and distinguished.
    - 439. Formation of contract of subscription in general.
    - 440. Consideration-Mutuality-Contract under seal.
    - 441. Incomplete subscriptions.
    - 442. Subscription distinguished from agreement to subscribe.
    - 443. A subscription paper as an agreement between subscribers.
    - 444. Agreements to pay to agent or trustee for proposed corporation.
    - 445. Form of subscription, and formalities in subscribing.
    - 446. Subscription or agreement implied from conduct.
    - 447. Effect of mistake.
    - 448. Capacity of subscribers, and effect of disability.
    - 449. Subscriptions made through agent and by partner.
    - 450. Authority and duties of persons receiving subscriptions.
    - 451. Revocation or withdrawal of subscriptions.
    - 452. Lapse of subscriptions.
    - 453. Illegality of subscriptions.
    - 454. Proof of subscriptions.
- II. SUBSCRIPTIONS UPON EXPRESS CONDITIONS PRECEDENT, IMPLIED CONDITIONS PRECEDENT, AND CONDITIONAL DELIVERY OF SUBSCRIPTIONS.
  - § 455. In general.
    - 456. Conditional subscriptions defined.
    - 457. Conditional subscriptions distinguished from subscriptions upon special terms.
    - 458. Validity of conditions precedent.
    - 459. Effect of unauthorized conditional subscriptions.
    - 460. Oral conditions affecting written subscriptions.
    - 461. Effect of valid conditional subscriptions.
    - 462. Implied conditions precedent.
    - 463. Waiver of conditions and estoppel.
    - 464. Conditional delivery of subscriptions.
- III. SUBSCRIPTIONS UPON SPECIAL TERMS.
  - § 465. In general.
    - 466. Definition and effect.
    - 467. Power to accept subscriptions upon special terms, and validity thereof.

- IV. FRAUD IN PROCURING SUBSCRIPTIONS.
  - § 468. In general.
    - 469. Effect of fraud in general.
    - 470. Want of authority on part of person making representation.
    - 471. What amounts to fraud in procuring subscriptions.
    - 472. Remedies of subscriber.
    - 473. Limitations on right to rescind.
- V. WITHDRAWAL, RELEASE, AND DISCHARGE OF SUBSCRIBERS.
  - § 474. In general.
    - 475. Withdrawal.
    - 476. Release by corporation.
    - 477. Discharge by payment.
    - 478. Discharge by transfer.
    - 479. Discharge in bankruptcy.
    - 480. Discharge by alteration of contract.
    - 481. Discharge by nonperformance of conditions or special terms.
    - 482. Discharge by alteration or amendment of charter.
    - 483. Formation of different corporation.
    - 484. Discharge by consolidation.
    - 485. Special agreements with, release of, and nonpayment by, other stockholders.
    - 486. Exercise of powers granted by charter or general law.
    - 487. Mismanagement of corporation—Illegal election of officers, etc.
    - 488. Failure to comply with provisions of charter or general law—Ultra vires acts.
    - 489. Nonuser-Abandonment of enterprise.
    - 490. Delay in making calls-Statute of limitations.
- VI. REMEDIES OF CORPORATION AGAINST SUBSCRIBERS.
  - § 491. In general.
    - 492. Action on subscriptions.
    - 493. Forfeiture or sale of shares.
    - 494. Effect of forfeiture or sale.
    - 495. Remedies in case of unauthorized or irregular forfeiture or sale.
    - 496. Set-off and counterclaim by subscribers.
- VII. CALLS OR ASSESSMENTS ON UNPAID SUBSCRIPTIONS.
  - § 497. In general.
    - 498. When calls are necessary.
    - 499. Validity and sufficiency of calls.
    - 500. Notice of calls, and demand of payment.
- VIII. ASSIGNMENT, MORTGAGE, OR PLEDGE OF UNPAID SUBSCRIPTIONS.
  - § 501. In general.
  - IX. INTEREST ON SUBSCRIPTIONS.
    - § 502. In general.
  - X. SUBSCRIPTION OF FULL AMOUNT OF CAPITAL STOCK OR OF SPECIFIED PERCENTAGE THEREOF.
    - § 503. In general.

- 504. As a condition precedent to incorporation, or to commencement of business.
- 505. As a condition precedent to liability on subscriptions.
- 506. What subscriptions may be counted.
- 507. Waiver and estoppel.
- XI. PAYMENTS ON SUBSCRIPTIONS.
  - § 508. In general.
    - 509. Effect of nonpayment on legality of incorporation or right to commence business.
    - 510. Effect of nonpayment on validity of subscriptions and liability of subscribers.
    - 511. Sufficiency of payment.
- XII. OVERSUBSCRIPTION AND APPORTIONMENT OR DISTRIBUTION OF STOCK.
  - § 512. In general.
    - 513. Effect of oversubscription.
    - 514. Distribution or apportionment.
- XIII. ESTOPPEL OF SUBSCRIBERS.
  - § 515. In general.
  - I. NATURE AND FORMATION OF CONTRACTS OF SUBSCRIPTION, AND OTHER AGREEMENTS.
- § 437. In general.—A subscription to the capital stock of a corporation is a contract between the corporation and the subscriber, and its formation and validity are governed by the same principles as any other contract, except in so far as such principles may be rendered inapplicable, or special formalities prescribed, by the charter or enabling act, or other statutes. As a general rule, both mutual assent and a consideration are essential.

If the corporation is in existence, a contract of subscription is formed by a simple offer and acceptance, like any other contract.

A subscription to the stock of a corporation to be subsequently formed cannot constitute a contract prior to the formation of the corporation, but is a mere offer, and may be revoked or withdrawn, or may lapse, unless made irrevocable by statute, at any time before the corporation is formed. Unless it is withdrawn or lapses, however, it is a continuing offer, and becomes a binding contract between the corporation and the subscriber as soon as the corporation is formed, and expressly or impliedly accepts the same.

The validity and effect of a subscription to the capital stock of a corporation is governed by the law of the state or country by or under whose laws the corporation was created.\*

<sup>\*</sup> Fish v. Smith, 73 Conn. 377; v. Morse, 44 App. Div. (N. Y.) 435. Bank of China, Japan & The Straits

### § 438. Subscriptions and other contracts defined and distinguished.

A contract of subscription to the stock of a corporation is a contract by which the subscriber agrees to take, and does take, a certain number of shares of the capital stock of a corporation, paying for the same, or expressly or impliedly promising to pay for the same. A writing reciting: "We, the undersigned subscribers, hereby bind ourselves to purchase the number of shares of stock set opposite our respective names in the Lincoln Shoe Manufacturing Company, at fifty dollars per share; to be paid," etc., as set forth in the writing, -is a contract of subscription. The effect of such a contract, as we shall see, the company being in existence at the time of the subscription, and having accepted the same, and the subscription being unconditional, is to make the subscriber a stockholder in the corporation, and to bind him to pay for his stock in accordance with the terms of his contract.

A subscription for stock, and a contract to purchase stock from a corporation, are not the same, and, as we have seen, they are to some extent governed by different rules. A contract for the sale of stock does not make the purchaser a subscriber or a stockholder until it is executed by delivery of the stock.2 Whether a particular contract is a subscription or a sale of stock depends upon its terms and the intention of the parties. The fact that the word "sale" or "purchase" is used is not conclusive.3

don. 44 Neb. 279.

<sup>2</sup> See ante, §§ 378b, 382.

to purchase the number of shares Co., 80 Ill. 446, 22 Am. Rep. 199. of stock set opposite our respec-

1 Lincoln Shoe Mfg. Co. v. Shel- rectors,"-it was held that this was a contract of subscription, and not a purchase of stock. See, also. <sup>3</sup> In Lincoln Shoe Mfg. Co. v. Wemple v. St. Louis, Jerseyville & Sheldon, 44 Neb. 279, where a writ-ing recited: "We, the undersigned wego & F. R. V. R. Co. v. Black, subscribers, hereby bind ourselves 79 Ill. 262; Melvin v. Lamar Ins.

An agreement by a contractor on tive names in the Lincoln Shoe a railroad to take an amount of Manufacturing Company at fifty the capital stock of the railroad dollars per share; one-fourth of company equal to one-fourth of the the amount so subscribed \* \* \* amount received for work under to be paid when the foundation of the contract is an agreement to the building is laid; one-fourth subscribe for the stock to that when the building is under roof, amount, and not to take it in part and the balance on call of the dipayment for the work. McMahon

A contract of subscription is also to be distinguished from an agreement to subscribe in the future. A subscription, when it becomes binding by acceptance, makes the subscriber a stockholder, and liable to calls for the full amount subscribed; but a contract to subscribe in the future does not make one a stockholder, but the remedy of the corporation, upon a breach thereof by refusal to subscribe, is by an action to recover damages for the breach, the measure of damages being, not the full amount of the promised subscription, but the difference between such amount and the value of the stock at the time of the hreach.4

A contract of subscription is also to be distinguished from a contract by which a person promises that another shall subscribe for shares. Such a contract does not make the promisor a subscriber, but merely renders him liable to the corporation, if the other does not subscribe, for the actual damages sustained by the corporation.5

A contract of subscription is also distinguishable from a contract between a number of persons by which they agree, merely between themselves, to form a corporation, and take stock therein, not intending a contract with the corporation when formed.

Y. 463. Compare Kelley v. Collier, 11 Tex. Civ. App. 353.

On the other hand, where a contract provided that the maker, for a specified consideration, a part of which was a delivery to him by a railroad company of a specified number of shares of its capital stock, would pay to a contractor of installments, and that the contract was not a contract of subscription to the capital Clark v. stock of the company. Continental Imp. Co., 57 Ind. 135.

stock in a corporation without any notice of a fraudulent contract beits officers, under which all its § 442.

v. New York & Erie R. Co., 20 N. stock has already been issued to such officer, to be by him transferred to subscribers on payment to him of forty per cent. of its par value, the existence of the agreement does not change him from a subscriber to an assignee of the stock. Bates v. Great Western Telegraph Co., 134 Ill. 536.

A bona fide purchaser of shares the company a certain sum in from original holders cannot be the regarded as subscribers because the whole thereof on completion of the shares, which have been voted but company's roadbed, it was held not issued to the vendors, are issued directly to the purchasers. Young v. Erie Iron Co., 65 Mich. 111.

4 Thrasher v. Pike County R. Where a person subscribes for Co., 25 Ill. 393. And see post, § 442.

5 Rhey v. Ebensburg & S. Planktween the corporation and one of Road Co. 27 Pa. St. 261. See post, On such a contract, the corporation, not being a party thereto, cannot maintain an action.<sup>6</sup>

An ordinary contract of subscription is also distinguishable from a contract by which a number of persons agree between themselves to form a corporation and take stock therein, and pay the amount of their several subscriptions to an agent or trustee for the corporation. The agent or trustee may sue them on such a contract, and, having collected the money, he will be liable to the corporation therefor.<sup>7</sup>

Whether a contract between a person and a corporation is a contract of subscription or a loan by the former to the latter depends entirely upon the terms of the contract and the intention of the parties, and is purely a question of fact, unless the intention is to be determined from a construction of a written contract, or an oral contract as to the terms of which there is no dispute. An absolute agreement to take a certain number of shares in a corporation, and pay for them in installments, is not a loan to the corporation on the stock as collateral, as distinguished from a subscription, because the subscriber or the corporation is given an option to resell or repurchase the stock within a certain time.

## § 439. Formation of contract of subscription.

(a) In general.—A contract of subscription for stock in a corporation, when binding, is a contract between the subscriber or subscribers and the corporation, and its formation and validity are governed by the same principles, substantially, as any other contract, except in so far as such principles may be rendered inapplicable by particular charter or statutory provisions. No person can become a stockholder in a corporation by virtue of a subscription for stock, in the absence of elements of estoppel, unless there is a valid contract between him and the cor-

<sup>&</sup>lt;sup>6</sup> Lake Ontario Shore R. Co. v. <sup>8</sup> McComb v. Barcelona Apart-Curtiss, 80 N. Y. 219. See post, § ment Ass'n, 134 N. Y. 598. 443. <sup>9</sup> Melvin v. Lamar Ins. Co., 80

<sup>&</sup>lt;sup>7</sup> West v. Crawford, 80 Cal. 19; Ill. 446, 22 Am. Rep. 199. San Joaquin Land & Water Co. v. <sup>10</sup> Melvin v. Lamar Ins. Co., 80 West, 94 Cal. 399. See post, § 444. -Ill. 446, 22 Am. Rep. 199.

poration. No particular formalities are necessary, unless by reason of express charter or statutory provisions, but a contract is always essential; and a valid contract involves an offer and acceptance of the offer, or mutual assent of the subscriber and the corporation. Whenever this element is wanting, there is no valid subscription.11

"Although it may be true," said the Indiana court in a late case, "that a binding contract of subscription to the stock of a corporation, unless the statute or articles of association provide to the contrary, may be made, without actually signing a formal subscription paper or stock book, in any manner that the subscriber and corporation clearly manifest their purpose to enter into a contract whereby the relation of stockholder of the corporate stock is to result—yet there must in every case be some sort of subscription or contract whereby the subscriber obtains the right, upon some condition, to demand stock and to exercise the rights of a stockholder. Contracts for membership in a corporation are not different in their essential elements from other contracts. There must be contracting parties whose minds mutually assent to some proposition, and whose agreement creates corresponding obligations between the parties."12

Whether a subscription is made before or after the formation of the corporation, it is formed by an offer by one of the parties,—the corporation or the subscriber, as the case may be,—and an acceptance of this offer by the other. As soon as an offer to take shares made by a person to a corporation is accepted by the corporation, or as soon as an offer of shares by a corporation is accepted by the person to whom it is made, there is a binding contract of subscription, under which the

<sup>11</sup> Butler University v. Scoonover, 114 Ind. 381, 5 Am. St. Rep.
627; Oldtown & Lincoln R. Co. v.
Veazie, 39 Me. 571; Plank's Tavern Co. v. Burkhard, 87 Mich. 182;
White v. Kahn, 103 Ala. 308; Glenn
v. Garth, 133 N. Y. 18; Rochester
er, 114 Ind. 381, 5 Am. St. Rep.
& Kettle Falls Land Co. v. Roe, 7 627.

subscriber, without any further act on the part of himself or the corporation (unless required by statute), becomes a stockholder, with all the rights, and subject to all the liabilities, arising from such a relation.13

(b) Subscription after corporation is formed.—In the case of subscriptions after a corporation has been formed and is in existence, there is no difficulty in the formation of the contract. There must simply be both an offer and an acceptance, as in the case of any other contract. When a corporation solicits subscriptions to its stock, intending merely to solicit the submission of subscriptions, a subscription is like an offer in the formation of any other contract. Until it is accepted by the corporation, or an authorized agent of the corporation, there is no contract, and neither party is bound.14 As soon, however, as the corporation accepts it, there is from that moment a binding contract, on the part of the subscriber, in most jurisdictions. 15 to pay the amount of the subscription and assume the other liabilities of a stockholder, and upon the part of the corporation to issue a proper certificate of stock, and to admit him to all the rights and privileges of a stockholder, in accordance with the express and implied terms of the contract. In other words, the subscriber becomes, by virtue of the subscription and its acceptance, a stockholder, with all the rights, and subject to all the liabilities, common law and statutory, which belong or attach to stockholders.16

17 Am. St. Rep. 910; California see Pittsburgh & Connellsville R. Southern Hotel Co. v. Callender, Co. v. Plummer, 37 Pa. St. 413. 94 Cal. 120, 28 Am. St. Rep. 99; 15 Post, § 492. Walter A. Wood Harvester Co. v. Robbins, 56 Minn. 48; and cases (N. Y.) 20, 28 Am. Dec. 513; Incited in the notes following. (N. Y.) 20, 28 Am. Dec. 513; Instead in the notes following.

<sup>13</sup> See Spear v. Crawford, 14 Badger Paper Co. v. Rose, 95 Wis. Wend. (N. Y.) 20, 28 Am. Dec. 513; 145; Carter, Rittenberg & Hainlin Chester Glass Co. v. Dewey, 16 Co. v. Hazzard, 65 Minn. 432; Co-Mass. 94, 8 Am. Dec. 128; Cart-zart v. Herndon, 114 N. C. 252; wright v. Dickinson, 88 Tenn. 476, Gilman v. Gross, 97 Wis. 224. And

tone of the notes following.

14 Oldtown & Lincoln R. Co. v. Bibb (Ky.) 576, 5 Am. Dec. 638;

Veazie, 39 Me. 571; Starrett v. Taggart v. Western Maryland R. Rockland Fire & Marine Ins. Co., Co., 24 Md. 563, 89 Am. Dec. 760;

65 Me. 374; Junction R. Co. v. Chester Glass Co. v. Dewey, 16

Reeve, 15 Ind. 236; Stuart v. Valley R. Co., 32 Grat. (Va.) 146; wright v. Dickinson, 88 Tenn. 476,

A solicitation of subscriptions by a corporation may be intended, not merely as an invitation to submit subscriptions for acceptance by the corporation, but as an offer of stock by the corporation to any person who may subscribe in accordance with the terms of the offer. In such a case, a subscription in accordance with the terms of the offer is an acceptance of the offer, and creates a binding contract, from which neither party can withdraw without the consent of the other. Such is the case, for example, when a corporation opens subscription books, and puts them in the hands of an agent to receive subscriptions, and a person enters his name therein as a subscriber for a certain number of shares. This makes a binding contract of subscription.17

A subscription for stock need not be accepted by the corporation in any particular way, unless this is required by the charter or statute, or expressly or impliedly by the subscription itself, but may be inferred by the conduct of the corporation in entering it in its books, retaining it, demanding payment, or otherwise acting upon it.18

When subscriptions are made to the stock of a corporation, and are accepted by the corporation by a formal vote of the directors, entered upon the records of the corporation, the subscriptions become binding immediately upon such acceptance, without any notice to the subscribers, unless such notice is required by the express or implied terms of the subscription.19 But the subscription may, from its nature or the circumstances under which it is made, require notice of acceptance.20

In England, a formal written application for shares is made

<sup>17</sup> Am. St. Rep. 910; Richmond-ville Union Seminary v. McDon-ald, 34 N. Y. 379; Mobile & Ohio R. Co. v. Yandal, 5 Sneed (Tenn.) 294.

Ill. 248, 33 Am. St. Rep. 234.

<sup>17</sup> Greer v. Chartiers Ry. Co., 96 to this case, see post, § 451(b). Dec. 337. Compare Pittsburgh & Connellsville R. Co. v. Plummer, 37 Pa. St. 413.

<sup>19</sup> New Albany & Salem R. Co. v. Pa. St. 391, 42 Am. Rep. 548. As McCormick, 10 Ind. 499, 71 Am.

<sup>20</sup> Cozart v. Herndon, 114 N. C.

by persons desiring to take shares in a joint-stock company, and it is well settled that the application is a mere offer, which must be accepted before either the applicant or the company is bound. Until the company accepts the offer and allots the shares to the applicant, and gives him notice of the acceptance and allotment, there is no contract, and neither party is bound.<sup>21</sup> An uncommunicated acceptance is not enough. The shares must be allotted by the directors, and notice thereof given to the applicant, or put in a way to be communicated to him as contemplated by the application.<sup>22</sup> Unless some other notice or method of communication is required by the applicant, notice may be communicated by mail, and in such a case the acceptance and notice take effect, and the contract is made, at the moment a letter of acceptance is deposited in the mail, properly addressed and stamped, although it may be delayed in reaching the applicant, or may never reach him, the postoffice being the agent of the applicant to communicate the acceptance.23

(c) Subscriptions before corporation is formed.—There has been some difficulty in settling the principles governing subscriptions to the stock of a corporation before its formation; but it is now well settled that when persons sign an agreement to form a corporation, and to take stock therein, intending a contract with the corporation,24 the subscription of each of the parties is a continuing offer to the proposed corporation, and becomes a binding contract as soon as the corporation is formed, and expressly or impliedly accepts the same. The fact that

<sup>&</sup>lt;sup>21</sup> Ramsgate Victoria Hotel Co. Pellatt's Case, 2 Ch. App. 527; In v. Montefiore, L. R. 1 Exch. 109; re Peruvian Ry. Co., 4 Ch. App. In re Portuguese Consolidated Copper Mines, 42 Ch. Div. 160; Hebb's Case, L. R. 4 Eq. 9; Harris' Case, 7 Ch. App. 587; In re Peruvian Ry. Co., 4 Ch. App. 322; Pellatt's Case, 2 Ch. App. 527; Household Fire & Carriage Accident Ins. Co. v. Grant, 4 Exch. Div. 216; In re Brewery Assets Corp., [1894] 3 Ch. 272.

<sup>&</sup>lt;sup>22</sup> Hebb's Case, L. R. 4 Eq. 9;

<sup>322;</sup> Harris' Case, 7 Ch. App. 587; Adams' Case, L. R. 13 Eq. 474; Household Fire & Carriage Accident Ins. Co. v. Grant, 4 Exch. Div.

<sup>23</sup> Household Fire & Carriage Accident Ins. Co. v. Grant, 4 Exch. Div. 216; Harris' Case, 7 Ch. App.

<sup>24</sup> See post, § 442.

the corporation is not in existence at the time the offer is first made by signing the agreement does not prevent the formation of the contract by its acceptance of the offer when formed.25

"In agreements of this nature, entered into before the organization is formed, or the agent constituted to receive the amounts subscribed, the difficulty is to ascertain the promisee, in whose name alone suit can be brought. The promise of each subscriber 'to and with each other,' is not a contract capable of being enforced, or intended to operate literally as a contract to be enforced, between each subscriber all the others collectively as individuals. The undertaking is inchoate and incomplete as a contract until the contemplated organization is effected, or the mutual agent constituted to represent the association of individual rights in accepting and acting upon the propositions offered by the several subscriptions. When thus accepted, the promise may be construed to

<sup>25</sup> Penobscot R. Co. v. Dummer, Busey, 5 Mackey (D. C.) 233; 40 Me. 172, 63 Am. Dec. 654; Athol Lackey v. Richmond & L. Turn-Music Hall Co. v. Carey, 116 Mass. pike Road Co., 17 B. Mon. (Ky.) 471; Chester Glass Co. v. Dewey, 16 Mass. 94, 8 Am. Dec. 128; Ma-Turnpike Road Co., 85 Ky. 184; rysville Electric Light & Power Co. Taggart v. Western Maryland R. v. Johnson, 93 Cal. 538, 27 Am. St. Co., 24 Md. 563, 89 Am. Dec. 760; Rep. 215; Minneapolis Threshing Hughes v. Antietam Mfg. Co., 34 Machine Co. v. Davis, 40 Minn. Md. 316; Red Wing Hotel Co. v. 110, 12 Am. St. Rep. 701; Hudson Real Estate Co. v. Tower, 156 Mass. 82, 32 Am. St. Rep. 434; Richelieu Hotel Co. v. Internation-Richelieu Hotel Co. v. Internation Curry Hotel Co. v. Mullins, 93 al Military Encampment Co., 140 Mich. 318; Bryant's Pond Steam III. 248, 33 Am. St. Rep. 234; Johns-Mill Co. v. Felt, 87 Me. 234, 47 Am. ton v. Ewing Female University, St. Rep. 323; Kimmins v. Wilson. 35 Ill. 518; Cross v. Pinckneyville 8 W. Va. 584; Stone v. Great West-Mill Co., 17 Ill. 54; Tonica & Peerr Oil Co., 41 Ill. 85; San Joaquin tersburg R. Co. v. McNeely, 21 Ill. Land & Water Co. v. Beecher, 101 71; Buffalo & New York City R. Cal. 70; Nickum v. Burckhardt, 30 Co. v. Dudley, 14 N. Y. 336; Amer- Or. 464, 60 Am. St. Rep. 822; Mc-Co. v. Dudley, 14 N. Y. 336; Amer-Or. 464, 60 Am. St. Rep. 822; Meican Silk Works v. Salomon, 4 Naught v. Fisher (C. C. A.) 96 Hun (N. Y.) 135; Dorris v. French, Fed. 168; Yonkers Gazette Co. v. 4 Hun (N. Y.) 292; Hamilton & D. Taylor, 30 App. Div. (N. Y.) 334. Plank Road Co. v. Rice, 7 Barb. (N. See, also, Griswold v. Board of Y.) 157; Penobscot R. Co. v. White, Trustees of Peoria University, 26 uelot Boot & Shoe Co. v. Hoit. 56 v. Trustees of Pre-emption Presby-N. H. 548; Melvin v. Hoitt, 52 N. terian Church, 110 Ill. 125; Edin-H. 61; Danbury & Norwalk R. Co. boro' Academy v. Robinson, 37 Pa. v. Wilson, 22 Conn. 435; Glenn v. St. 210, 78 Am. Dec. 421.

43; Bullock v. Falmouth & C. H. Friedrich, 26 Minn. 112; International Fair & Exposition Ass'n v. Walker, 83 Mich. 386, 88 Mich. 62;

41 Me. 512, 66 Am. Dec. 257; Ash- Ill. 41, 79 Am. Dec. 361; Whitsitt

have legal effect according to its purpose and intent, and the practical necessity of the case; to-wit, as a contract with the common representative of the several associates."26

A subscription to stock in a corporation to be formed cannot constitute a binding contract before the corporation is formed, for, in the first place, two parties are necessary to a contract, and, in the second place, until the corporation is formed, and expressly or impliedly accepts the subscription, there is no consideration or mutuality.<sup>27</sup> By the weight of authority, therefore, as we shall see in a subsequent section, a subscriber for stock in a corporation to be afterwards formed may revoke his subscription, and thus prevent a contract with the corporation, at any time before the corporation is formed, unless the subscription is made binding by statute.28

Notice of the acceptance by a corporation of a subscription made before its organization is not necessary. Nor need there be any formal acceptance. An acceptance may be inferred from the conduct of the corporation in retaining the subscription paper in its possession, and expending money or incurring debts on the faith of it.29

(d) Formation of a different corporation.—Since there must be mutual assent to constitute a binding contract of subscription, an offer to one person or corporation cannot be accepted by another. And it necessarily follows that a person who subscribes for stock in a corporation to be formed, and who does

26 Wells, J., in Athol Music Hall Co. v. Carey, 116 Mass. 471.

27 Strasburg R. Co. v. Echternacht, 21 Pa. St. 220, 60 Am. Dec. 49; Hudson Real Estate Co. v. Co. v. De La Green, 143 Pa. St. 269; Starrett v. Rockland Fire & Marine Ins. Co., 65 Me. 374; Knox v. Childersburg Land Co., 86 Ala.

The corporation must be organized within a reasonable time, or subscribers will be released. See post, § 452.

If the law is so changed before formation of the corporation that the object of the agreement cannot be carried into effect, the subscribers will not be liable. It was so Tower, 156 Mass. 82, 32 Am. St. held where, after subscriptions pay-Rep. 434; Muncy Traction Engine able in land, and before formation of the corporation, a statute was passed requiring all subscriptions to be payable in money. Knox v. Childersburg Land Co., 86 Ala. 180. 28 Post, § 451a.

<sup>29</sup> Richelieu Hotel Co. v. International Military Encampment Co., 140 Ill. 248, 33 Am. St. Rep. 234. See supra, this section, (b).

not consent to any change in the subscription, is not liable if the corporation which is afterwards formed, and which seeks to enforce the subscription, is a different corporation from that contemplated by the subscription. In such a case, no contract at all is formed.30

For this reason, where a number of persons sign a paper agreeing to take stock in a corporation to be formed under a general law, and some of the parties, on refusal of a certificate of incorporation by the attorney general under the general law. procure from the legislature a special act of incorporation, the corporation cannot enforce the subscriptions against the parties not consenting, since it is not the corporation contemplated by them. And it makes no difference that the corporation is created for the same purposes as were contemplated.31 The principle also applies where the corporation, although formed under the law under which it was intended to be formed. is formed for other purposes or with other powers than those contemplated by the subscribers; 32 or for a longer period; 33

Co., 25 Ill. 393; Greenbrier Industrial Exposition v. Rodes, 37 W. Va. 738; Norwich Lock Mfg. Co. v. Hockaday, 89 Va. 557; Craig Silver Co. v. Smith, 163 Mass. 262; Marysville Electric Light & Power Co. v. Johnson, 109 Cal. 192, 50 Am. St. Rep. 34; Baker v. Ft. Worth Board of Trade, 8 Tex. Civ. App. 560: Knottsville Roller Mill Co. v. Mattingly, 18 Ky. Law Rep. 246; Knox v. Childersburg Land Co., 86

A mere change in the name of the proposed corporation on its organization is immaterial, if there is no change in its character or objects. Yonkers Gazette Co. v. Tay- and for the purpose, as stated in lor, 30 App. Div. (N. Y.) 334.

a subscriber for stock in a pro- ning fruits and other products, and

30 Richmond Factory Ass'n v. posed corporation may be estopped Clarke, 61 Me. 351; Ticonic Water to set up the fact that the corpora-Power & Manufacturing Co. v. tion was formed for a different pur-Lang, 63 Me. 480; Machias Hotel pose or for a longer period than Co. v. Coyle, 35 Me. 405, 58 Am. that specified in the subscription. Dec. 712; Dorris v. Sweeney, 60 N. Greenbrier Industrial Exposition v. Y. 463; Thrasher v. Pike County R. Squires, 40 W. Va. 307, 52 Am. St. Rep. 884; Nickum v. Burckhardt, 30 Or. 464, 60 Am. St. Rep. 822. And see post, § 515.

31 Richmond Factory Ass'n v. Clarke, 61 Me. 351.

32 In Dorris v. Sweeney, 60 N. Y. 463, it was held that there was no liability on a subscription for stock in a corporation for the purpose of purchasing a patent for the purpose of preserving fruit and other products out of season, erecting a building, and stocking it with fruits to be preserved, where the corporation was formed under the general law authorizing the formation of manufacturing companies, its articles of association, of man-By participation or acquiescence. ufacturing preserved fruits, canwhere the corporation is formed under the laws of a different state than the one contemplated; 34 where the charter or certificate of incorporation fixes or authorizes a larger capital stock than is provided for in the subscription, or authorizes a larger capital stock, and creates the corporation for different objects; 35 or where the subscription is for stock in an unincorporated joint-stock company, and the association is incorporated.<sup>36</sup>

## § 440. Consideration—Mutuality—Contract under seal.

In the absence of provision to the contrary in the charter of a corporation or the general law, a subscription to its capital stock is not binding unless there is a consideration. In this respect, it is like any other contract. Obviously there must be mutuality of obligation, as in other bilateral contracts. for any reason the corporation is not bound, the subscriber is not bound, and vice versa. "A stock subscription," said Judge Campbell in a Michigan case, "is a transaction between the subscriber and the company, and the obligation of one can only be sustained by the corresponding obligation of the other. If both are not bound, neither is bound, and the transaction is a nullity." 37 It has been held, therefore, that where an oral sub-

preserving and keeping fruits and only, that it might, under the act other articles from decay. See, al- of incorporation, have carried on so, Norwich Lock Mfg. Co. v. Hockaday, 89 Va. 557; Baker v. Ft. Worth Board of Trade, 8 Tex. Civ. App. 560; Knox v. Childersburg Land Co., 86 Ala. 180.

A corporation formed for the purpose of "producing electricity and power" cannot enforce a preliminary subscription for stock in a corporation to be formed for the purpose of "furnishing the incandescent system of electric lighting." Marysville Electric Light & Power Co. v. Johnson, 109 Cal. 192, 50 Am. St. Rep. 34.

It has been held, however, that it is no defense to an action on a subscription by a company organized to carry on the business contemplated in the subscription pa-

other business. Haskell v. Worthington, 94 Mo. 560.

33 Greenbrier Industrial Exposition v. Rodes, 37 W. Va. 738.

That the subscriber may be estopped, see note 30, supra.

34 Craig Silver Co. v. Smith, 163 Mass. 262.

35 Baker v. Ft. Worth Board of Trade, 8 Tex. Civ. App. 560; Norwich Lock Mfg. Co. v. Hockaday, 89 Va. 557; Newport Cotton-Mill Co. v. Mims, 103 Tenn. 465; Middlecoff Hotel Co. v. Yeomans, 89 Ill. App. 170.

36 Machias Hotel Co. v. Coyle, 35 Me. 405, 58 Am. Dec. 712; Knottsville Roller Mill Co. v. Mattingly. 18 Ky. Law Rep. 246.

. 37 Carlisle v. Saginaw Valley & per, and engaged in that business St. Louis R. Co., 27 Mich. 315. And scription for stock is not binding upon the corporation, and does not make the subscriber a stockholder, because a statute requires subscriptions to be in writing, a note given in payment of such a subscription is void for want of consideration.38 Where a corporation is not bound by a subscription because of want of authority on the part of the person who accepted the same, the subscriber is not bound.39 A subscription for stock in a telephone company, or a note given in payment therefor, is void for want of consideration, where the business of the company is an infringement.40

If a subscription has been accepted by the corporation, or an offer of shares by the corporation has been accepted by subscribing, and statutory or charter requirements have been complied with, there is a sufficient consideration for the promises of both parties; the subscriber's promise to pay his subscription being supported by the corporation's obligation to recognize him as a stockholder, and pay him his proportion of any dividends, etc., or by its agreement to construct works or carry out the undertaking, or by the payment of money, or incurring of obligations, etc., and the promises on the part of the corporation being supported by the subscriber's promise, express or implied, to pay his subscription.41

37 Ohio St. 339, 41 Am. Rep. 517; 23; New York & Minnesota Gold Min. Co. v. Martin, 13 Minn. 417; Macedon & B. Plank-Road Co. v. Snediker, 18 Barb. (N. Y.) 317.

lins, 8 Mass. 292.

Bank, 53 Ark. 512. 41 Worcester Turnpike Corp. v. Willard, 5 Mass. 80, 4 Am. Dec. 39; Instone v. Frankfort Bridge Co., 2 Bibb (Ky.) 576, 5 Am. Dec. 638;

see Fanning v. Hibernia Ins. Co., Griswold v. Board of Trustees of Peoria University, 26 Ill. 41, 79 Essex Turnpike Corp. v. Collins, 8 Am. Dec. 361; Walter A. Wood Mass. 292; Parker v. Northern Harvester Co. v. Robbins, 56 Minn. Central Michigan R. Co., 33 Mich. 48; Minneapolis & St. Louis R. Cc. v. Bassett, 20 Minn. 535, 18 Am. Rep. 376; Danbury & Norwalk R. Co. v. Wilson, 22 Conn. 435; First Nat. Bank of Cedar Rapids v. Hur-38 Fanning v. Hibernia Ins. Co., 37 Ohio St. 339, 41 Am. Rep. 517. 39 Essex Turnpike Corp. v. Col-85 Ky. 184; Kennebec & Portland ns, 8 Mass. 292. R. Co. v. Jarvis, 34 Me: 360; Ken-40 Clemshire v. Boone County nebec & Portland R. Co. v. Palmer, 34 Me. 366; Bish v. Bradford, 17 Ind. 490; Society of Middlesex Husbandmen & Manufacturers v. Davis, 3 Metc. (Mass.) 133; Hayne v. Beauchamp, 5 Smedes & M. Selma & Tennessee R. Co. v. Tip- (Miss.) 515; Thigpen v. Mississipton, 5 Ala. 787, 39 Am. Dec. 344; pi Central R. Co., 32 Miss. 347;

In some of the cases, as we shall see, agreements by a number of persons to form a corporation, and take stock therein when formed, have been regarded as agreements between the subscribers, so as to render each promise a consideration for the others.42 But this view is not supported by the weight of authority.43

Subscriptions under seal.—Since, at common law, a promise or undertaking under seal requires no consideration to support it, a subscription under seal is binding, where the corporation is in existence, although it has not been accepted, and there is no consideration, in all states in which the commonlaw doctrine still obtains.44 In most states, however, the doctrine that an agreement under seal is binding without any consideration has been abolished by statute, or is not recognized.

### § 441. Incomplete subscriptions.

Strictly speaking, an incomplete subscription is no subscription at all. In order that there may be a binding subscription, the parties must, as in the case of other contracts, have reached a complete agreement. If anything remains to be agreed upon or done, there is no contract.45

It follows that a person who, prior to the formation of a corporation, signs an informal subscription paper, with the understanding that it is not final, but merely to see what can be

Osborn v. Crosby, 63 N. H. 583; Ft. lips Limerick Academy v. Davis, 11 Edward & Ft. M. Plank-Road Co. v. Payne, 17 Barb. (N. Y.) 567; Hamilton & D. Plank-Road Co. v. Rice, 7 Barb. (N. Y.) 157; Buffalo & New York City R. Co. v. Dudley, 14 N. Y. 336; Lake Ontario, Auburn & N. Y. R. Co. v. Mason, 16 N. Y. 451; Ohio Wesleyan Female College v. Higgins, 16 Ohio St. 20; Rhey v. Ebensburg & S. Plank-Road Co., 27 Pa. St. 261; Gibbons v. Grinsel, 79 Wis. 365.

42 Post, § 443; Marysville Electric Light & Power Co. v. Johnson,

Mass. 113, 6 Am. Dec. 162.

44 See Hudson Real Estate Co. v. Tower, 156 Mass. 82, 32 Am. St. Rep. 434. See post, § 451(c).

45 See Ridgway v. Wharton, 6 H. L. Cas. 268; Winn v. Bull, 7 Ch. Div. 29; Mercer County Court v. Kentucky River Navigation Co., 8 Bush (Ky.) 300; Oldtown & Lincoln R. Co. v. Veazie, 39 Me. 571; White v. Kahn, 103 Ala. 308; First Universalist Society in Newburytric Light & Power Co. v. Johnson, 93 Cal. 538, 27 Am. St. Rep. 215; 417; Plank's Tavern Co. v. Johnson, Twin Creek & C. Turnpike Road hard, 87 Mich. 182; Strasburg R. Co. v. Echternacht, 21 Pa. St. 220, port v. Currier, 3 Metc. (Mass.) 417; Plank's Tavern Co. v. Burkdone towards the enterprise, and that a formal subscription paper will be presented later, and who refuses to sign the latter paper when presented, is not liable as a subscriber on the formation of the company.46

It also follows that, to render one liable as a subscriber for stock in a corporation by reason of his having signed a subscription paper or articles of association, the paper must be "A signature to an incomplete paper," said Judge Johnson in a New York case, "wanting in any substantial particular, when no delegation of authority is conferred to supply the defect, does not bind the signer, without further assent on his part, to the completion of the instrument." 47

Articles of association, in which blanks are left for the names of directors, or for any other statements required by the statute, are not complete, and a person who has signed the same in such condition is not liable thereon as a subscriber when the blanks are afterwards filled in without his consent.48 been held, however, that, when persons sign a subscription book for the purpose of influencing other persons to subscribe, with the number of shares to be taken left blank, so that they may afterwards withdraw their subscriptions, the agents of the corporation may fill in the blank, and render their subscriptions binding.49

### Subscription distinguished from agreement to subscribe § 442. in the future, or agreement that another shall subscribe.

There is undoubtedly a distinction between a subscription to the stock of a corporation to be formed, which, when the corporation is formed and accepts the same, will make the subscriber a stockholder, without any further act on his part, and a mere agreement to subscribe when the corporation shall be formed, although it may sometimes be difficult to ascertain the

<sup>46</sup> Plank's Tavern Co. v. Burkhard, 87 Mich. 182. And see White v. Kahn, 103 Ala. 308. Newall, 3 Fost. & F. 130; McClelard v. Whiteley, 15 Fed. 322.

R. Co. v. Mabbett, 58 N. Y. 397.

48 Dutchess & Columbia County

Co., 101 Ill. 57.

intention of the parties, and determine whether a particular agreement is the one or the other. Where the agreement is of the latter character, there is no contract of subscription, making the party a stockholder; or entitling the corporation to maintain an action against him as a subscriber, until he has carried out the agreement by formally becoming a subscriber on the books of the corporation, or otherwise. The only remedy of the corporation, in case of the party's refusal to subscribe in accordance with the agreement, is an action against him for damages for breach of the agreement, and the measure of damages is not necessarily the par value of the stock agreed to be taken, but the actual loss sustained by the corporation. This distinction was made in an Illinois case, in which persons subscribed an instrument reciting: "We, the undersigned, agree to subscribe to the stock of the Pike County Railroad the sums set against our names, when the books may be opened for subscription." It was held that this was not a subscription for stock, making the signers stockholders in the corporation, and liable to calls, but a mere executory agreement to subscribe when the subscription books should be opened, for breach of which the company could only claim as damages the actual loss sustained by it, which, as a general rule, is the difference between the actual value and the par value of the stock.<sup>50</sup>

The difficulty with respect to this distinction between subscriptions and agreements to subscribe in the future is in construing particular agreements, and ascertaining the intention of the parties. It is competent, of course, for a person to agree to subscribe for the stock of a projected corporation when it shall be organized, so that he will not be liable as a subscriber

50 Thrasher v. Pike County R. corporation and the corporation, Co., 25 Ill. 393, 405. See, also, modifying a provise in his sub-quick v. Lemon, 105 Ill. 578; Mt. scription by changing the amount Sterling Coalroad Co. v. Little, 14 to be subscribed by others as a Bush (Ky.) 429, as to which, how-ever, see infra, this section; Char-lotte & South Carolina R. Co. v. scription into an agreement to sub-Blakely, 3 Strob. (S. C.) 245. An agreement between a sub-Jackson & P. R. Co., 31 Ohio St. An agreement between a sub- Jackson & P. R. Co., 31 Ohio St. scriber to the capital stock of a 23.

without a formal subscription after the corporation is organized, instead of making a present subscription which will render him liable as a subscriber as soon as the corporation is organized, without any further action on his part; and when this appears to have been the intention of the parties, the courts must construe the agreement accordingly. Ordinarily, however, when persons sign a subscription paper, agreeing to take a certain number of shares in a corporation to be formed, their intention is to bind themselves as subscribers, and to become stockholders as soon as the corporation is formed, and not merely to agree to formally subscribe after the corporation has been formed; and therefore, unless a contrary intention clearly appears, an instrument by which the signers agree to take shares in a corporation when formed should be construed, not as a mere agreement to subscribe in the future, but as a continuing offer to the corporation to take shares, which, when the corporation is formed and accepts the same, becomes a binding contract of subscription, giving the corporation a right of action against the subscribers, as such, for the amount of their subscriptions.51

In a Kéntucky case, where persons signed an instrument reciting: "The undersigned propose to subscribe for the number of shares of \$50 each to the capital stock of the Mt. Sterling Coalroad Company, when the charter shall have been obtained and the company organized, provided that the company receives our subscriptions, payable" in certain specified installments,—it was held, following the Illinois case above referred to, that this was not a subscription, but a mere agreement to subscribe in the future, for breach of which the company's remedy was an action to recover as damages the actual loss sustained. In a later decision, however, this case was overruled, and it was held that an agreement to subscribe one thousand dollars to the capital stock of a turnpike road company, and to

<sup>51</sup> See the cases cited ante, § 439.
52 Mt. Sterling Coalroad Co. v. And see Yonkers.Gazette Co. v. Taylor, 30 App. Div. (N. Y.) 334.

pay the same as soon as the company should be organized, and the construction of its road commenced, was a binding contract of subscription when accepted by the corporation, and not a mere agreement to subscribe in the future.<sup>53</sup>

Agreement that another shall subscribe.—A contract by which one person promises that another person shall subscribe for stock in a corporation is not in any sense a contract of subscription by the promisor, so as to render him liable for the full amount of the promised subscription if the other refuses to subscribe. And it is immaterial that he expressly promises to be personally responsible for such subscription. Such a contract, if, indeed, it is not void for impossibility of performance and want of consideration,54 is a contract for which the remedy of the corporation, in case the promised subscription is not procured, is an action for damages, the measure of damages being not the full amount of the promised subscription, but the actual loss,—the difference between the amount of the subscription and the value of the stock.55

## § 443. A subscription paper as a contract between the subscribers.

It has been said that, when a number of persons sign a subscription paper by which they agree to take shares in a corporation to be subsequently formed by them, there is a contract between the subscribers, which cannot be revoked.<sup>56</sup> But,

Turnpike Road Co., 85 Ky. 184. See, also, North Missouri R. Co. v. Miller, 31 Mo. 19; Mobile & Ohio R. Co. v. Tandal, 5 Sneed (Tenn.) 294. And see the cases cited under section 439, supra.

54 It would seem that the promise in such a case is impossible of performance, since the other person cannot be made to subscribe, and is therefore no consideration for the contract on the part of the corporation; and if the corporation is Ass'n v. Walker, 83 Mich. 386; not bound, the promisor is not Twin Creek & C. Turnpike Road bound. See Clark, Contracts, 182; Co. v. Lancaster, 79 Kv. 552; Glenn Harvy v. Gibbons, 2 Lev. 161; Ste-v. Busey, 5 Mackey (D. C.) 233.

58 Bullock v. Falmouth & C. H. vens v. Coon, 1 Pin. (Wis.) 356; Ward v. Hollins, 14 Md. 158.

> 55 Rhey v. Ebensburg & S. Plank-Road Co., 27 Pa. St. 261.

> 56 1 Morawetz, Priv. Corp. §§ 45, 47, 50. And see Minneapolis Threshing Machine Co. v. Davis, 40 Minn. 110, 12 Am. St. Rep. 701 (post, § 192); Marysville Electric Light & Power Co. v. Johnson, 93 Cal. 538, 27 Am. St. Rep. 215; International Fair & Exposition

as a rule, this is not true. Whether there is such a contract depends upon the intention of the parties. Of course it is possible for persons to enter into a contract with each other individually to form a corporation and take stock therein, and if such an intention appears, the courts must construe the contract accordingly.<sup>57</sup> Ordinarily, however, the parties signing a subscription paper do not intend to contract with each other individually, but intend to contract with the corporation when formed. When this is the intention, the agreement must be so construed,—not as a case of mutual promises, but as so many separate continuing offers to the proposed corporation, which must be expressly or impliedly accepted by the corporation before any contract can result.<sup>58</sup> This is true, even when the promise and agreement of the subscribers is in terms "to and with each other," as is sometimes the case. It was said in a leading Massachusetts case: "The promise of each subscriber 'to and with each other' is not a contract capable of being enforced, or intended to operate literally as a contract to be enforced between each subscriber and each other who may have signed previously, or who should sign afterwards, nor between each subscriber and all the others collectively as individuals. The undertaking is inchoate and incomplete as a contract until the contemplated organization is effected, or the mutual agent constituted to represent the association of individual rights in accepting and acting upon the propositions offered by the several subscriptions. When thus accepted, the promise may be construed to have legal effect according to its purpose and intent, and the practical necessity of the case; to wit, as a contract with the common representative of the several associates." 59

When there is a contract between the individuals signing a

v. Curtiss, 80 N. Y. 219.

<sup>58</sup> See Trustees of Phillips Limerick Academy v. Davis, 11 Mass. 116 Mass. 473. 113, 6 Am. Dec. 162; Athol Music If a number of persons sign a

<sup>57</sup> See Lake Ontario Shore R. Co. ant's Pond Steam Mill Co. v. Felt, 87 Me. 234, 47 Am. St. Rep. 323.

<sup>59</sup> Athol Music Hall Co. v. Carey,

Hall v. Carey, 116 Mass. 473; Bry- subscription paper merely agree-

subscription paper to take stock in a corporation to be formed, as distinguished from a continuing offer by each subscriber to the proposed corporation, the contract, at common law, cannot be enforced by the corporation when formed. It cannot be enforced by the corporation unless it was made for its benefit, and the law in the particular jurisdiction allows a person for whose benefit a contract is made to sue thereon, although not a party to the contract. In a New York case, a number of persons signed a subscription paper reciting: "We the undersigned, citizens of Unionville and vicinity, pledge ourselves to subscribe for and take stock in and for the construction of the Lake Ontario Shore Railroad, to the amount set opposite our names respectively, on condition said road be located and built through or north of the village of Unionville," etc. The court of appeals held that this was not a contract of subscription between the signers of the instrument and the railroad company, but an agreement between the signers only, to which the company was not in any sense a party, and that the company, therefore, could not maintain an action thereon.60

If a subscription paper be regarded as constituting both a contract between the subscribers as individuals and a continuing offer to the proposed corporation, as it may be if such an intention appears, a breach by one of the signers by withdrawing before formation of the corporation would merely give the others, as individuals, a right of action for any damages sustained by them. There is no principle upon which it can be

academy, the promises are void, for want of a promisee; and an action to recover the subscriptions cannot be maintained on the agreement by a corporation subsequent—

60 Lake Ontario Shore R. Co. v. Curtiss, 80 N. Y. 219, 222. See Trustees of Phillips Limerick Acadly created by the legislature for emy v. Davis, 11 Mass. 113, 6 Am. the purpose of erecting the acade- Dec. 162.

ing to pay a certain sum each for my. The fact that the act of inerecting an academy, without corporation authorizes the corporaagreeing to pay the same to any tion to receive and hold all moneys particular person, and without pro- subscribed in trust for the acadvision for the formation of a cor- emy is immaterial, for the legislaporation to receive the amount of ture cannot create a promise on the subscriptions and erect the the part of the subscribers without their assent. Trustees of Philboth for want of consideration, and lips Limerick Academy v. Davis, 11 Mass. 113, 6 Am. Dec. 162.

held that, after such a breach, his offer would continue so as to be open for acceptance by the corporation when formed.<sup>61</sup>

# § 444. Agreements to pay to agent or trustee for proposed corporation.

Instead of subscribing directly for stock in a proposed corporation, so as to create a contract between the subscribers and the corporation when formed, a number of persons may enter into a mutual agreement to form a corporation and take stock therein, and to pay the amounts which they agree to subscribe to a certain person as agent or trustee. Such an agreement is a valid contract between the parties, being a case of mutual promises, and their liability to pay is not affected by the fact that they have not subscribed articles of incorporation in compliance with the statute under which the corporation is formed. or by the fact that it has not yet been formed, unless this is required by the contract.<sup>62</sup> Under such a contract as this, the agent or trustee, as the trustee of an express trust, may maintain an action against the subscribers on their several promises, and collect the money for the use of the corporation.<sup>63</sup> when the trustees have collected the money, the corporation, for whose use the money has been received, may maintain an action against them to recover the same.64

The person so designated as payee is the agent or trustee of the subscribers prior to the organization of the corporation, but after the corporation is formed, he becomes its agent or trustee, and not the agent or trustee of the subscribers. And since he has no interest coupled with the agency, the corporation may remove him at any time, and appoint another in his place, or itself assume the custody and disposition of the money.<sup>65</sup>

<sup>61</sup> The contrary was held in a late Minnesota case, but the decision cannot be sustained. See post, § 451(a).

<sup>63</sup> West v. Crawford, 80 Cal. 19.64 San Joaquin Land & Water Co.v. West, 94 Cal. 399.

<sup>65</sup> San Joaquin Land & Water Co. v. West, 94 Cal. 399

<sup>62</sup> West v. Crawford, 80 Cal. 91. v. West, 94 Cal. 399.

### Form of subscription and formalities in subscribing.

(a) In general.—Unless the charter of a corporation, or the general law under which it is organized, requires that subscriptions shall be in some particular form, or that they shall be made with certain formalities, no other form or formality is necessary to a valid subscription than is required for any other simple contract. 66

The contract, of course, must be sufficiently definite and certain to enable a court to enforce it. An indefinite subscription for stock in a corporation to be formed, for example, which does not specify the amount of stock of the corporation, or what proportion the subscriber is to take, or when or by whom the company is to be organized, cannot be enforced.<sup>67</sup> It is well settled, however, that the fact that a subscription paper is informal does not render the subscriptions invalid, if the intention of the parties can be ascertained. "Whatever may be the form or language of a subscription to the stock of an incorporated company, any person who in any manner becomes a subscriber for or engages to take any portion of the stock of such company, thereby assumes to pay for the same according to the

66 Nulton v. Clayton, 54 Iowa, 425, 37 Am. Rep. 213; Rensselaer & W. Plank Road Co. v. Barton. 16 N. Y. 460, note; Fry v. Lexington & Big Sandy R. Co., 2 Metc. (Ky.) 314; Gill v. Kentucky & C. Gold & Silver Min. Co., 7 Bush (Ky.) 635; York Park Bldg. Ass'n v. Barnes, 39 Neb. 834; Ross v. Bank of Gold Hill, 20 Nev. 191; Phoenix Warehousing Co. v. Badger, 6 Hun (N. Y.) 293, 67 N. Y. 294; Chamberlain v. Painesville & Hudson R. Co., 15 Ohio St. 225; Brownlee v. Ohio, Indiana & Illi-nois R. Co., 18 Ind. 68; Griswold v. Seligman, 72 Mo. 110; Wellersburg & West Newton Plank Road Co. v. Young, 12 Md. 476; Musgrave v. matter will not render a subscrip-Morrison, 54 Md. 161; Belknap v. tion invalid. Agricultural Branch Adams, 49 La. Ann. 1350; Barron R. Co. v. Winchester, 13 Allen v. Burrill, 86 Me. 66; Anderson v. (Mass.) 29.

Scott (N. H.) 49 Atl. 568; Walter v. Merced Academy Ass'n, 126 Cal. 582; Corwith v. Culver, 69 III. 502.

Subscriptions are not invalid because the subscribers, in signing, use initials for their Christian names. State v. Beck, 81 Ind. 500.

A receipt for a certificate of stock written in the margin of a subscription book is a sufficient subscription. Lohman v. New York & Erie R. Co., 2 Sandf. (N. Y.) 39.

67 Nemaha Coal & Min. Co. v. Little, 54 Kan. 424; Loutsenhizer v. Farmers' & Merchants' Milling Co., 5 Colo. App. 479.

Uncertainty as to an immaterial

conditions of the charter." 68 "It matters not how informal the writing may be, if the intent of the parties can be collected from it." 69 Where a subscription paper is incomplete, any omissions may be explained by parol evidence. 70 A writing reciting an association for the purpose of organizing a corporation, and "the number of shares held by each" of the persons signing the same, imports and is sufficient as a subscription by each signer for the number of shares set opposite his name.<sup>71</sup> Subscriptions are not rendered invalid because there is no dollar mark before the figures representing the sums agreed to be paid, 72 or the number of shares is not expressly stated, where the intention in this respect otherwise appears.<sup>73</sup> Misnomer of a corporation in a subscription for its stock does not render the subscription invalid, if the intention of the parties is shown.74

(b) Form or formalities required by charter or statute.—Sometimes the charter of a corporation or the general law under which it is formed expressly requires that subscriptions to its capital stock shall be in a certain form, or made with certain formalities, and, unless the provisions can be regarded as merely directory, 75 a subscription not in the prescribed form, or not entered into with the prescribed formalities, is invalid, and not enforceable either by the subscriber or by the corporation, 76 in

Some courts, as we shall see in another section, hold that there can be no action on a subscription unless there is an express promise to pay. See post, § 492.

69 Nulton v. Clayton, 54 Iowa, 425, 37 Am. Rep. 213.

70 Espy v. Mt. Lebanon Cemetery, 1 Walk. (Pa.) 40. See post, § 454. 71 Nulton v. Clayton, 54 Iowa, 425, 37 Am. Rep. 213.

72 Richelieu Hotel Co. v. Interna-

68 Rensselaer & W. Plank Road shares of stock are fixed at \$100. Co. v. Barton, 16 N. Y. 460, note. Haskell v. Sells, 14 Mo. App. 91; Columbus Land Co. v. McNally, 172 Pa. St. 158.

74 Hager's Town Turnpike Road Co. v. Creeger, 5 Har. & J. (Md.) 122, 9 Am. Dec. 495; Milford & C. Turnpike Co. v. Brush, 10 Ohio, 111; Oler v. Baltimore & Randallstown R. Co., 41 Md. 583. And see ante, § 52.

75 See infra, this section, (h). 76 Carlisle v. Saginaw Valley & St. Louis R. Co., 27 Mich. 315; Fantional Military Encampment Co., 110 III. 248, 33 Am. St. Rep. 234.

78 A subscription of \$1,000 in a corporation to be formed is not void for failure to designate the number of shares, where the st. Co., 27 Mich. 515, Fair-tional Nilitary Encampment Co., 27 Mich. 515, Fair-tional Nilitary Encampment Co., 27 Mich. 515, Fair-tional Nilitary Encampment Co., 37 Ohio St. 2018 Ins. Co., 27 Mich. 515, Fair-tional Nilitary Encampment Co., 38, Fair-tional Nilitary Encampment Co., 10 Nilitary Encampment Co., 10 Nilitary Encampment Co., 110 Ni the absence of elements of estoppel.<sup>77</sup> "No person can obtain rights of membership in a corporation except in compliance with its charter or governing law, and if that prescribes any conditions or special methods of becoming a member, the law is imperative. There may be cases of mutual dealing which will estop both parties, but no contract or subscription can be valid if not conforming to the statute."78

It is generally in the case of subscriptions preliminary to or at the time of the organization of corporations that the legislature prescribes formalities; but they may also be required in the case of subscriptions after a corporation has been formed. In a Michigan case, where a statute authorized formation of a corporation, and declared that all persons subscribing the articles of association, "and all other persons who shall, from time to time thereafter, subscribe to or become the holders of the capital stock of said corporation, in the manner to be provided by its by-laws," should be a body corporate, it was held that a subscription could only be made in the manner provided by the by-laws of the corporation, and that a subscription made before any by-laws were adopted on the subject was a nullity.79

The fact that a subscription in the form prescribed by the charter or statute contains additional stipulations not inconsistent with the charter or statute, and which are valid at common law, does not invalidate the subscription.80

A subscriber, by acting as a stockholder, may be estopped to set up informalities in his subscription.81

(c) Necessity for writing-Statute of frauds.-No writing at all is necessary to a valid subscription to the stock of a corporation unless it is expressly or impliedly required by the charter or the general law under which the corporation is formed. In the absence of such a requirement, a valid subscription may be

Ind. 342; Coppage v. Hutton, 124 79 Carlisle v. Saginaw Valley & Ind. 401; and other cases cited in St. Louis R. Co., 27 Mich. 315. the notes following.

<sup>77</sup> See post, § 515.78 Carlisle v. Saginaw Valley & St. Louis R. Co., 27 Mich. 315, 318. 565. See post, § 515.

<sup>80</sup> Fisher v. Evansville & Craw-

fordsville R. Co., 7 Ind. 407. 81 Lane v. Brainerd, 30 Conn.

made either orally or in writing, or partly orally and partly in writing,82 or it may be implied from conduct.83 A subscription in writing, however, may be expressly or impliedly required by the charter or general law, and in such a case, an oral subscription cannot be enforced 84 unless there is an estoppel.85 In an Ohio case, where the general law authorizing the formation of corporations provided for the opening of books by commissioners to receive subscriptions to stock prior to organization, and for organization and the election of directors after the amount of stock specified in the certificate of association should be subscribed, it was held that a verbal subscription was invalid, that it did not give the subscriber any rights as against the corporation when formed, and that there was no consideration, therefore, for a note given by him to the corporation in payment of the subscription.86

-Statute of frauds.-A subscription for stock in a corporation is not within the statute of frauds, either as an agreement for the sale of goods, wares, or merchandises, or, when the corporation owns land, as an agreement for the sale of land, or an interest therein.87

s2 Cookney's Case, 3 De Gex & Pa. St. 340; Greenbrier Industrial J. 170; Colfax Hotel Co. v. Lyon, Exposition v. Rodes, 37 W. Va., 738; 834; Shellenberger v. Patterson, N. 160. 168 Pa. St. 30; Webb v. Baltimore 85 Po & Eastern Shore R. Co., 77 Md. 92, 39 Am. St. Rep. 396; Barron v. Burrill, 86 Me. 66; Walter v. Merced Academy Ass'n, 126 Cal. 582.

The contrary was intimated, but without any citation of authority, in Ingersoll & Thamesford Gravel Road Co. v. McCarthy, 16 U. C. Q. made improvements on the faith of

83 Post, § 446.

84 Vreeland v. New Jersey Stone Co., 29 N. J. Eq. 188; Fanning v. Hibernia Ins. Co., 37 Ohio St. 339, 41 Am. Rep. 517; Pittsburgh & Shore R. Co., 77 Md. 92, 39 Am. St. Steubenville R. Co. v. Gazzam, 32 Rep. 396; York Park Bldg. Ass'n

69 Iowa, 683; Bullock v. Falmouth Coyote Gold & Silver Min. Co. v. 8 C. H. Turnpike Road Co., 85 Ky. Ruble, 8 Or. 284; Galveston Hotel 184; Tabler v. Anglo-American Co. v. Bolton, 46 Tex. 633; New Ass'n, 17 Ky. Law Rep. 815; York Brunswick & Canada Railway & Park Bldg. Ass'n v. Barnes, 39 Neb. Land Co. v. Muggeridge, 4 Hurl. &

85 Post, § 515.

An oral subscriber is estopped to deny the validity of his subscription on the ground that it was not in writing, where he has recognized it as valid by postponing the time of payment, and the corporation has entered into contracts and it. Perkiomen Brick Co. v. Dyer, 187 Pa. St. 470.

86 Fanning v. Hibernia Ins. Co., 37 Ohio St. 339, 41 Am. Rep. 517. 87 Webb v. Baltimore & Eastern

A contract to subscribe for shares is within the statute as an agreement not to be performed within a year from the making thereof, if by its terms it is not to be performed within a year. But it is otherwise if it may be performed within a year, although it is not in fact performed within that time. An agreement to subscribe for stock when the books of the corporation shall be opened for subscription is not within the statute of frauds as an agreement not to be performed within a year, where the books may be opened within a year.88 The same is true of a contract of subscription to the stock of a railroad company, to be performed when the construction of its road is commenced, where it may be commenced within a year.89

(d) Requirement of formal articles of association.—Sometimes the general law authorizing the formation of a corporation requires that the subscribers to its stock, in organizing the corporation, shall subscribe formal articles of association, setting forth the amount of the capital stock, the number of shares subscribed by each, and various other matters. And it has been held in some states under such a statute that a person who subscribes for stock, either orally, or by signing a preliminary subscription paper, but who does not sign the formal articles of association, as provided by the statute, does not become a stockholder and cannot be held liable on his subscription.90 In a New York case, a general law authorizing the formation of

v. Barnes, 39 Neb. 834; Rogers v. R. Co., 50 Ind. 342. See, also, Bu-Burr, 105 Ga. 432. And see post, § cher v. Dillsburg & Mechanicsburg 610.

 <sup>88</sup> Gadsden v. Lance, 1 McMul.
 Eq. (S. C.) 87, 37 Am. Dec. 548. 89 Bullock v. Falmouth & C. H.

Turnpike Road Co., 85 Ky. 184. 90 Poughkeepsie & Salt Point Plankroad Co. v. Griffin, 24 N. Y. 150; Dutchess & Columbia County R. Co. v. Mabbett, 58 N. Y. 397; Troy & Boston R. Co. v. Tibbits, 18 Barb. (N. Y.) 297; Sedalia, Warsaw & Southern Ry. Co. v. Wilkerers for stock in an existing corpo-

son, 83 Mo. 235; Monterey & Salinas Valley R. Co. v. Hildreth, 53 Cal. 123; Reed v. Richmond Street St. Rep. 230.

R. Co., 76 Pa. St. 306; Coppage v. Hutton, 124 Ind. 401; Shick v. Citizens' Enterprise Co., 15 Ind. App. 329, 57 Am. St. Rep. 230.

Compare Ft. Edward & Ft. M. Plank Road Co. v. Payne, 17 Barb. (N. Y.) 567; Buffalo & Jamestown R. Co. v. Clark, 22 Hun (N. Y.)

ration. Shick v. Citizens' Enterprise Co., 15 Ind. App. 329, 57 Am.

plank road and turnpike companies required subscription books to be opened, notice thereof given, subscriptions received, election of directors, etc., and then declared that the subscribers should "thereupon severally subscribe articles of association," in which should be set forth the name of the company, and It further declared that each subcertain other particulars. scriber to the articles of association should subscribe his name. residence, and the number of shares taken by him, that the articles should be filed in the office of the secretary of state, and that "thereupon the persons who have so subscribed, and all persons who shall, from time to time, become stockholders in such company, shall be a body corporate," etc. Under this statute, it was held that persons who merely signed a preliminary subscription paper, and did not subscribe the articles of association, did not become stockholders, and were not liable on the subscriptions.91

In some states, such statutes have been construed differently. and subscriptions otherwise than by signing the formal articles of association have been sustained.92 In order that subscriptions may be binding, the subscribers need not sign the formal articles of association or certificate of incorporation, unless there is some express requirement to this effect in the charter or general law.\*

Defects in the articles will not necessarily render the subscription invalid.93

(e) Signing subscription book.—A person is not liable as a subscriber by reason of his signing a subscription paper or of

road Co. v. Griffin, 24 N. Y. 150.

92 Peninsular R. Co. v. Duncan, 28 Mich. 130; Greenbrier Industrial Exposition v. Rodes, 37 W. Va. 738. And see San Joaquin Land & Water Co. v. Beecher, 101 Cal. 70.

In an Indiana case it was held that, while one who subscribes for stock in a corporation, by signing preliminary articles, may perhaps refuse to sign the subsequent formal articles of association required N. Y. 185.

91 Poughkeepsie & S. P. Plank- by statute, yet where the required number of persons sign the formal articles, and they are duly recorded, the corporation thus created may recover from a subscriber of the preliminary articles only. Johnson v. Wabash & Mt. V. Plank-Road Co., 16 Ind. 389.

> \* See Yonkers Gazette Co. v. Taylor, 30 App. Div. (N. Y.) 334.

93 Cayuga Lake R. Co. v. Kyle, 64

an oral agreement, where he has not signed or authorized another to sign the subscription book, if subscription in this mode is required by statute.94 But signing the subscription book is not necessary unless it is required by statute. The mere fact that a statute authorizes subscription books to be opened does not prevent subscriptions in other modes.95

- (f) Acknowledgment of articles or agreement.—If the statute requires the formal agreement or articles of association to be acknowledged as well as signed, acknowledgment is essential. Where a general law provided that an agreement for the formation of a corporation thereunder should be acknowledged by the several corporators before a justice, and there was no such acknowledgment, although a certificate of incorporation was issued, it was held that no corporate existence was acquired as to persons who signed the preliminary agreement as subscribers for stock, but did not acknowledge the same, and that they were not liable on their subscriptions.96
- (g) Substantial compliance with charter or statute.—If there has been a substantial compliance with the requirements of the statute in subscribing for stock in a corporation, it is sufficient, and the subscriptions will not be rendered invalid because the statute was not strictly and literally complied with. A require-

94 Charlotte & South Carolina R. Co. v. Blakely, 3 Strob. (S. C.) 245; McClelland v. Whiteley, 15 Fed. 322; Woodruff v. McDonald, 33 Ark. 97; Shurtz v. Schoolcraft & Three Rivers R. Co., 9 Mich. 269; Parker v. Northern Central Michigan R. Co., 33 Mich. 23; Northern Central Michigan R. Co. v. Eslow, 40 Mich. 222. But see Mexican Gulf R. Co. v. Viavant, 6 Rob. (La.) 305.

As to substantial compliance with the charter or statute in this respect, see infra, this section, (g).

146; People v. Stockton & Visalia R. Co., 45 Cal. 306; Hamilton & D. Plank Road Co. v. Rice, 7 Barb. (N. Court v. Paris, W. & K. R. Turnpike Co., 11 B. Mon. (Ky.) 143; North Eastern R. Co. v. Rodrigues, 10 Rich. Law (S. C.) 278. See post, § 450(a).

96 Greenbrier Industrial Exposition v. Rodes, 37 W. Va. 738; Coppage v. Hutton, 124 Ind. 401.

The Indiana statute making it necessary for subscribers to sign 95 Buffalo & Jamestown R. Co. v. and acknowledge the articles of as-Gifford, 87 N. Y. 294; Brownlee v. sociation does not apply to sub-Ohio, Indiana & I. R. Co., 18 Ind. scriptions to the stock of existing 68; Ashtabula & New Lisbon R. corporations. Shick v. Citizens' En-Co. v. Smith, 15 Ohio St. 328; Stuterprise Co., 15 Ind. App. 329, 57 art v. Valley R. Co., 32 Grat. (Va.) Am. St. Rep. 230. ment that the subscribers shall sign formal articles of association, stating particular facts, is substantially complied with where each subscriber signs a separate paper, if the papers are all alike, and comply with the statute in the statement of facts.<sup>97</sup>

Where a pocket memorandum book was opened for subscriptions, and subscriptions entered therein before organization of the corporation, and the directors of the corporation, after its organization, adopted the book and accepted the subscriptions therein, with the assent of the subscribers, it was held that there was a substantial and sufficient compliance with a statutory requirement that the directors should, after the organization of the corporation, open books for subscriptions.<sup>98</sup>

Where subcriptions to the capital stock of a bridge company were made on a loose sheet of paper, which was put in a bound book used as a record of the company, and the contents of the paper, with the names of the subscribers and amounts subscribed, were entered in the book by the commissioners appointed to open books of subscription, it was held that there was a substantial and sufficient compliance with a statute requiring the opening of subscription books.<sup>99</sup>

(h) Provisions merely directory.—In order that subscriptions may be invalid because of failure to comply with provisions of the law under which the corporation is organized, the provisions must be mandatory, and not merely directory to the officers of the corporation. Where a general law authorizing the formation of railroad companies provided that, if the full amount of the capital stock should not be taken, the directors of the corporation, after the filing of the articles of association, might open subscription books and receive subscriptions for the stock not taken, it was held that the provision as to the mode of receiving the subscriptions was merely directory, and did not prevent the directors from receiving subscriptions in other modes than by signing on the books.<sup>100</sup>

<sup>97</sup> Lake Ontario, Auburn & N. Y. R. Co. v. Mason, 16 N. Y. 451. 97. 98 Buffalo & Jamestown R. Co. v. Gifford, 87 N. Y. 294.

#### § 446. Subscriptions implied from conduct.

When subscriptions are not required to be entered into in any particular form, a subscription may be implied from conduct. Thus, a person who accepts a certificate of stock from a corporation, or who acts as a stockholder by participating in stockholders' meetings, making payments, or otherwise, thereby becomes a stockholder, and liable as such, not only to creditors, but also to the corporation, although there may have been no express contract of subscription. 101

Acting as a director.—It was formerly held in England that, when qualification to act as a director of a corporation is made dependent upon ownership of a certain number of shares in the corporation, a person who acts as a director impliedly subscribes for the number of shares required to qualify him, and is liable to that extent on the winding up of the company.102 The later cases, however, hold that there is no such liability, unless qualification shares are allotted, or liability is expressly imposed by statute.103

#### § 447. Effect of mistake.

There are few decisions as to the effect of mistake upon a contract of subscription, but such a contract is governed by the

v. Gifford, 87 N. Y. 294. And see supra, this section, (d), (e).

101 Shickle v. Watts, 94 Mo. 410; Barron v. Burrill, 86 Me. 66; Up-ton v. Tribilcock, 91 U. S. 45, 1 Cum. Cas. 824; Chubb v. Upton, 95 U. S. 665. And see Ross v. Bank of Gold Hill, 20 Nev. 191; Griswold v. Seligman, 72 Mo. 110; Musgrave v. Morrison, 54 Md. 161; Anderson v. Scott (N. H.) 49 Atl. 568; Belknap v. Adams, 49 La. Ann. 1350; post, § 515.

102 In re Great Oceanic Telegraph Co., L. R. 13 Eq. 30; In re Empire Assur. Corp., 6 Ch. App. 469; In re British Colonial & Foreign Property Ins. Corp., 45 L. J. trian Printing & Publishing Union, Ch. 488.

103 In re Percy & Kelly Nickel, Cobalt & Chrome Iron Min. Co., 5 Ch. Div. 705; In re Medical Attendance Ass'n, 55 Law T. (N. S.) 612. Compare In re Portuguese Consolidated Copper Mines [1891] 3 Ch.

Where the charter of a corporation expressly provides that acting as a director shall be equivalent to a contract to pay for the number of shares necessary to qualify, one who so acts is liable upon required number of shares. although they may not have been allotted to him. In re Anglo-Aus-[1892] 2 Ch. 158.

same rules in this respect as any other contract. 104 The cases in which mistake has any effect at all upon the validity of a contract are limited. When it has any effect at all, it renders the contract void, and not merely voidable, as in the case of fraud. If a person, without negligence, enters into a contract of subscription under a mistake as to the nature of the transaction, induced by the deceit or other fault of a third person, against which ordinary diligence cannot guard, the subscription is void on the ground of mistake. 105 The same is true where a person subscribes for shares under a mistake as to the corporation, the subscription being made to the stock of one corporation, when it is intended to subscribe for stock in another. 106 As a rule, a mistake as to the subject-matter of a contract has no effect at all except where the mistake is (1) as to the existence of the subject-matter; (2) as to the identity of the subject-matter, where what is meant by each party answers the description of the subject-matter; (3) as to the essential nature or qualities of the subject-matter, where the mistake goes to the whole substance of the agreement, and renders the subject-matter contracted for essentially different in kind from the thing as it actually exists, and where the mistake is mutual; (4) as to quantity; and (5) as to price. 107

In a Massachusetts case, a subscriber for shares in a corporation, in an action by the corporation to recover an assessment thereon, set up as a defense that the published estimate of the powers and capacity of the corporation was erroneous, and that he would not have subscribed if he had known the facts. As there was no evidence of any intention to deceive those subscribing on the faith of the estimates, it was held that the defense could not be sustained. 108

<sup>104</sup> See Clark, Contracts, 289 et 105 See Clark, Contracts, 291; Foster v. Mackinnon, 4 C. P. 704. 28, 25 Am. Rep. 9.

<sup>&</sup>lt;sup>107</sup> See, generally, Clark, Contracts, 295 et seq.

<sup>108</sup> Salem Mill-Dam Corp. v. Ropes, 9 Pick. (Mass.) 187, 19 Am. 106 See Clark, Contracts, 293; Dec. 363. See, also, Crossman v. Humble v. Hunter, 12 Q. B. 311; Penrose Ferry Bridge Co., 26 Pa. Boston Ice Co. v. Potter, 123 Mass. St. 69, wherein it was held that a mistake as to the probable ex-

Mistake in subscribing for a greater number of shares than was intended is no ground for relief in equity, where the subscriber has allowed the corporation to act upon the faith of the subscription.<sup>109</sup>

Mistake due to ignorance of the law, as a mistake as to the legal effect of the contract, is clearly no ground for relief, either at law or in equity. But when a person, without negligence, is induced by fraud or false representations to sign a subscription paper in ignorance of its character or contents, as in the case of a blind or ignorant and illiterate person, he is not bound by the subscription. Some of the courts regard the subscription as merely voidable in such a case on the ground of fraud; but the better opinion is that it is absolutely void on the ground of mistake, for there is a mistake on the part of the subscriber, as well as fraud on the part of the corporation or its agents. 111

### § 448. Capacity of subscribers, and effect of disability.

(a) In general.—Unless there is some provision to the contrary in the charter of a corporation, or the law under which it is organized, the capacity of a person to subscribe for stock therein, and the effect of subscriptions by persons under legal disability, are governed by substantially the same rules as any other contract. The charter or statute may expressly or impliedly impose restrictions, or it may make one liable on

pense of the undertaking is no defense.

And see Chesapeake & Ohio Canal Co. v. Dulany, 4 Cranch, C. C. 85, Fed. Cas. No. 2,647; Payson v. Withers, 5 Biss. 269, Fed. Cas. No. 10,864 (mistake as to the condition of the company); Williams v. Thwing Electric Co., 160 Ill. 526 (where it was held that the fact that a person subscribed for stock in a proposed corporation, in the belief that it was an organized and existing corporation, the mistake being due to ignorance of the laws of the state in which it was located, was no ground for equitable relief).

<sup>109</sup> Diman v. Providence, Warren & B. R. Co., 5 R. I. 130.

110 Upton v. Tribilcock, 91 U. S. 45, 1 Cum. Cas. 45; Clem v. Newcastle & Danville R. Co., 9 Ind. 488, 68 Am. Dec. 653; New Albany & Salem R. Co. v. Fields, 10 Ind. 187. And see the cases cited post, § 471(e).

in a proposed corporation, in the belief that it was an organized and existing corporation, the mistake 223; Jackson v. Hayner, 12 Johns. being due to ignorance of the laws (N. Y.) 469; Foster v. Mackinnon, of the state in which it was located, was no ground for equitable v. Copley, 67 Pa. St. 386, 5 Am. Rep. 441.

a subscription who would not be liable at common law; but unless it does so, the general principles governing the capacity of parties to contract are applicable.112

(b) Subscriptions by infants.—In the absence of charter or statutory restrictions, there is nothing to prevent an infant from subscribing for stock in a corporation. But, as in the case of other contracts except those for necessaries, he may, at his option, disaffirm and repudiate his contract when he attains his majority, or before, and if he does so, he cannot be held liable either to the corporation or to creditors. 113

The right of an infant to disaffirm his contract of subscription is subject to the qualification, applicable to other contracts of infants, that he cannot do so if he has ratified the same, either expressly or impliedly, since attaining his majority. 114 And he does ratify it, and thus render it binding, if, after attaining his majority, he accepts the benefits of it, or acts upon it as a binding contract, as by receiving dividends, taking part in stockholders' meetings, or otherwise acting as a stockholder, or if he does not disaffirm the contract within a reasonable

v. Coombe, 3 Exch. 565; Phillips v. Covington & Cincinnati Bridge Co., 2 Metc. (Ky.) 219; Appeal of Hahn (Pa.) 7 Atl. 482.

(Pa.) 7 Atl. 482.

113 Newry & Enniskillen Ry. Co.
v. Coombe, 3 Exch. 565; North
Western Ry. Co. v. McMichael, 5
Exch. 114; Ebbett's Case, 5 Ch.
App. 302; Lumsden's Case, 4 Ch.
App. 31; Wilson's Case, L. R. 8 Eq.
240; Baker's Case, 7 Ch. App. 115;
Pim's Case, 3 De Gex & S. 11;
Hart's Case, L. R. 6 Eq. 512; Phillips v. Covington & Cincinnati Bridge Co., 2 Metc. (Ky.) 219. Where a minor subscribed for

shares in a proposed corporation, and received and paid for the same, and afterwards, before any business was entered into, the officers and stockholders formed a new corporation, and agreed to sell all the

112 Newry & Enniskillen Ry. Co. property of the original corpora-Coombe, 3 Exch. 565; Phillips v. tion to it, and wind up the affairs of the original corporation, and the new corporation, in consideration of the transfer to it, issued its shares to the stockholders of the old corporation, it was held that the minor could not rescind his subscription for the stock in the old company, and recover what he paid from the new corporation, as his contract was not with the latter. White v. Mount Pleasant Mills Corp., 172 Mass. 462.

> As to whether subscriptions by an infant can be counted in determining the amount of stock subscribed, see post, § 506.

> 114 Lumsden's Case, 4 Ch. App.31; Ebbett's Case, 5 Ch. App. 302; and cases cited in the notes follow

time. 115 If he does not elect to repudiate the contract within a reasonable time after attaining his majority, and manifest his intention to do so, he will be liable for calls made while he was an infant, as well as for those made afterwards. 116

- (c) Subscriptions by married women.—At common law, the contracts of a married woman, with few exceptions, are absolutely void, and this principle applies, except in so far as it has been changed by statute, to a married woman's subscription for stock in a corporation. 117 In most jurisdictions, however, the common-law doctrine as to a married woman's capacity to contract has been modified or altogether abolished, so that she may bind her separate estate by a contract of subscription, as well as by other contracts. 118
- (d) Subscriptions by or for the corporation itself, and subscriptions by other corporations.—A corporation may subscribe for shares of stock in another corporation, if it is expressly authorized to do so, or if such a contract is a necessary or proper means of accomplishing the purpose for which it was created.119 Ordinarily, however, as was shown in a former chapter, such a transaction is not within the powers of a corporation. 120 A statute merely authorizing a corporation

Thirsk Ry. Co. v. Fearnley, 4 Exch. 26; North Western Ry. Co. v. Mc-Michael, 5 Exch. 114.

31; Ebbett's Case, 5 Ch. App. 302.

Compare Hart's Case, L. R. 6 Eq. 512; Wilson's Case, L. R. 8 Eq. 240. 117 Pugh & Sharman's Case, L. R. 13 Eq. 566; National Commercial Bank v. McDonnell, 92 Ala. 387; Appeal of Hahn (Pa.) 7 Atl. 482; Phillips v. Covington & Cincinnati Bridge Co., 2 Metc. (Ky.)

118 Matthewman's Case, L. R. 3 Eq. 781; Witters v. Sowles, 32 Fed. Y. 9.

<sup>115</sup> Cork & Bandon Ry. Co. v. <sup>119</sup> Louisville & Nashville R. Co. Cazenove, 10 Q. B. 935; Leeds & v. Literary Society of St. Rose, 91 Ky. 395, where it was held that a literary corporation owning and operating a large farm, under authority conferred by its charter, had 116 North Western Ry. Co. v. McMichael, 5 Exch. 114; Dublin & the power to subscribe for stock in
Wicklow Ry. Co. v. Black, 8 Exch.
181; Mitchell's Cast, L. R. 9 Eq.
1863; Lumsden's Case, 4 Ch. App.
the farm, and was of great benefit to its operation, etc.

See, also, Mayor & City Council of Baltimore v. Baltimore & Ohio R. Co., 21 Md. 50; Tod v. Kentucky Union Land Co., 57 Fed. 47; Marbury v. Kentucky Union Land Co. (C. C. A.) 62 Fed. 335. And see ante, § 193 et seq.

120 Valley Ry. Co. v. Lake Erie Iron Co., 46 Ohio St. 44, 1 Keener's Cas. 815; Central R. Co. v. Pennsylvania R. Co., 31 N. J. Eq. 475; 767; In re Reciprocity Bank, 22 N. Franklin Co. v. Lewiston Institution for Savings, 68 Me. 43, 28 Am.

to "invest" its money "in real or personal property, stocks, or choses in action," gives it the power to invest in the stock of organized corporations, but does not authorize it to subscribe for stock in a projected corporation. 121

In most jurisdictions, an ultra vires subscription by a corporation for stock in another corporation is absolutely void, and cannot be enforced either by or against the corporation. 122

In organizing a corporation, subscriptions for stock cannot be made either in the name of the corporation itself, or in the name of others as agents or trustees for the corporation. 123

- (e) Subscriptions by municipal corporations.—A municipal corporation has no power to subscribe for shares in a private corporation unless there is a valid law authorizing it to do so; but the legislature may authorize a municipal corporation, or quasi corporation, like a city or county, to subscribe for stock in a railroad company or other quasi public corporation for the purpose of aiding it in the construction of its works. 124
- (f) Subscriptions by officers, agents, and commissioners.—In the absence of express charter or statutory restrictions, the officers of a corporation may subscribe for shares therein, provided

Rep. 9, 1 Keener's Cas. 504, 1 Cum. Compare, however, United States Cas. 343; Mechanics' & Working Vinegar Co. v. Foehrenbach, 148 Cas. 343; Mechanics' & Working Men's Mut. Sav. Bank & Bldg. Ass'n v. Meriden Agency Co., 24 Conn. 159; Pauly v. Coronado Beach Co., 56 Fed. 428; New Orleans, Florida & H. Steamship Co. v. Ocean Dry Dock Co., 28 La. Ann. 173, 26 Am. Rep. 90; Knowles v. Sandercock, 107 Cal. 629; Nassau Bank v. Jones, 95 N. Y. 115, 47 Am. Rep. 14, 1 Smith's Cas. 497, 2 Keener's Cas. 781; Berry v. Yates, 24 Barb. (N. Y.) 199; Peshtigo Co. v. Great Western Telegraph Co., 50 Ill. App. 624; Denny Hotel Co. v. Schram, 6 Wash. 134, 36 Am. St. Rep. 137; Commercial Fire Ins. Co. v. Board of Revenue, 99 Ala. 1, 42 Am. St. Rep. 17. And see ante, § 193.

121 Commercial Fire Ins. Co. v. Board of Revenue, 99 Ala. 1, 42 Am. St. Rep. 17.

122 See cases in note 120, supra. porations.

N. Y. 58.

123 Preston v. Grand Collier Dock Co., 11 Sim. 327; Holladay v. Elliott, 8 Or. 84; Johnston v. Allis, 71 Conn. 207.

In Johnston v. Allis, supra, it was held that one who subscribed for stock as "trustee" for the benefit of the proposed corporation, and afterwards, as one of the officers of the corporation, signed, published, and caused to be recorded a certificate of its organization, which set forth his subscription with the others, was personally liable on the subscription, on insolvency of the corporation, both on the ground that the subscription was not binding on the corporation, and on the ground of estoppel.

124 See works on municipal cor-

they do so fairly, and without violating the rights of, or perpetrating a fraud upon, other stockholders or subscribers. And commissioners appointed by a statute to open subscription books and receive subscriptions may become subscribers themselves. An agent in whose possession a subscription book is placed by the corporation for the purpose of soliciting and receiving subscriptions may subscribe himself by entering his name therein. 127

Neither the officers or agents of a corporation, however, nor the commissioners appointed to receive subscriptions, will be allowed to take advantage of their position to exclude others, and take a majority of the stock for the purpose of gaining control of the corporation, or otherwise in fraud of the rights of other stockholders.<sup>128</sup>

(g) Citizenship and residence.—In the absence of charter or statutory restrictions, a person who is otherwise capable of entering into a binding contract is not rendered incompetent to subscribe for stock in a corporation by the fact that he is a nonresident of the state, or an alien.<sup>129</sup> Generally, however, the statutes require that a certain number of the corporators shall be residents of the state, and such a provision is mandatory.<sup>130</sup>

## § 449. Subscriptions made through agents and by partners.

(a) In general.—A person may subscribe for shares in a corporation as the agent of another, provided there is no charter or statutory provision in the way, and provided he has author-

<sup>125</sup> Sims v. Street R. Co., 37 Ohio St. 556; Christopher v. Noxon, 4 Ont. (Can.) 672.

128 Walker v. Devereaux, 4 Paige (N. Y.) 229.

127 Greer v. Chartiers Ry. Co., 96
 Pa. St. 391, 42 Am. Rep. 548.

128 Brower v. Passenger Ry Co., 3 Phila. (Pa.) 161; Morris v. Stevens, 178 Pa. St. 563. See post, § 450(b).

<sup>129</sup> Com. v. Hemmingway, 131 Pa. St. 614.

130 Sword v. Wickersham, 29 Kan. 746; American Salt Co. v. Heidenheimer, 80 Tex. 344, 26 Am. St. Rep. 743.

As to the presumption, see ante, § 67(b).

As to de facto corporate existence in case of failure to comply with the charter or statute in this respect, see ante, \$ 82(g).

ity from the other to do so. And in such a case, the principal is entitled to the shares, and is liable on the subscription. 131 To bind the principal, the contract of subscription must have been in fact made by the agent. The mere fact that one is authorized to subscribe for another does not make the other a subscriber unless the authority is exercised by subscribing. 132

If a person assumes to act as agent for another in subscribing, when he is without authority, the person for whom he acts is clearly not bound unless ratification is shown, or unless he is estopped to deny the other's authority by having clothed him with apparent authority. 133 A person, however, for whom another has subscribed for shares without authority, may afterwards expressly or impliedly ratify the subscription, and thus render himself liable thereon, and entitled to its benefits.134

Philadelphia, Wilmington & B. R. Co. v. Cowell, 28 Pa. St. 329, 70 Am. Dec. 128. Compare Butler v. Merchants' Ins. Co., 14 Ala. 777.

132 See Grangers' Market Co. v.

Vinson, 6 Or. 172. 133 Ingersoll. & T. Gravel Road Co. v. McCarthy, 16 U. C. Q. B. 162; Pim's Case, 3 De Gex & S. 11; Rutland & Burlington R. Co. v. Lincoln, 29 Vt. 206; Ticonic Water Power & Manufacturing Co. v. Lang, 63 Me. 480; Drover v. Evans, 59 Ind. 454; Hume v. Commercial Bank, 9 Lea (Tenn.) 728; McClelland v. Whiteley, 11 Biss. 444, 15 Fed. 322; Merrick Thread Co. v. Philadelphia Shoe Mfg. Co., 115 Pa. St. 314; Brown v. Florida Southern Ry. Co., 19 Fla. 472; Coyote Gold & Silver Min. Co. v. Ruble, 8 Or. 284; Bucher v. Dillsburg & Mechanicsburg R. Co., 76 Pa. St. 306;

131 Burr v. Wilcox, 22 N. Y. 551; tended to be subscriptions to stock In re New York, Lackawanna & therein, and do not expressly au-W. Ry. Co., 99 N. Y. 12; Musgrave thorize the entry of their names v. Morrison, 54 Md. 161; State v. as subscribers, do not give author-Lehre, 7 Rich. Law (S. C.) 234; ity to the secretary of the company, when formed, to enter their names as stockholders. Coyote Gold & Silver Min. Co. v. Ruble, 8 Or. 284.

If a person signs a subscription book for stock in a proposed corporation for the purpose of inducing others to subscribe, leaving the amount of his own subscription blank, he impliedly authorizes those empowered to take subscriptions to fill up the blanks. As against other subscribers and creditors, he will be estopped to deny such authority. Jewell v. Rock River Paper Co., 101 Ill. 57.

134 Penobscot R. Co. v. Dummer, 40 Me. 172, 63 Am. Dec. 654; Musgrave v. Morrison; 54 Md. 161; Ticonic Water Power & Manufacturing Co. v. Lang, 63 Me. 480; Philadelphia, Wilmington & B. R. Co. v. Cowell, 28 Pa. St. 329, 70 Am. Dec. Chapman v. Virginia Real Estate
Investment Co., 96 Va. 177.

Agreements made by persons
contemplating becoming stockholdReno Savings Bank, 19 Nev. 103; ers in a corporation to be subse- Mississippi & Tennessee R. Co. v. quently formed, which are not in- Harris, 36 Miss. 17; McClelland v.

And ratification will be implied from recognition of the contract as binding, as where the person for whom it was made is elected and acts as a director or other officer, when he is not eligible unless he is a stockholder, or if he pays assessments, receives dividends, or attends stockholders' meetings, etc. 135 It has been held, however, that ratification by a person of an unauthorized subscription by another in his name is not to be implied from his subsequent declarations to strangers that he has taken that amount of stock. 136

If an agent subscribes in his own name, but for his principal, and there is no special charter or statutory provision preventing such a subscription, 137 nor any estoppel, 138 the principal is bound by the subscription, and he will be entitled to the benefit of it, both as against the corporation and as against the agent. 139 And if the agent is subjected to liability to creditors of the corporation or to the corporation by reason of the subscription, he may recover the amount paid from the principal.140

(b) Liability of pretended agent.—Whether a person who assumes to act as the agent of another in subscribing for stock is himself liable, when he has no authority, and when the subscription is not ratified by the person for whom he acts, is a question upon which the courts have differed. In some states it has been held that he becomes himself a subscriber and stockholder, and is liable as principal on the subscription, just as if he had assumed to act for himself.141 And they apply the same

Whiteley, 11 Biss. 444, 15 Fed. 322; Boggs v. Olcott, 40 Ill. 303; In re Hemp, Yarn & Cordage Co. (Hind-

ley's Case) [1896] 2 Ch. 121.

135 Penobscot R. Co. v. Dummer, 40 Me. 172, 63 Am. Dec. 654; Bogss v. Olcott, 40 III. 303; In re Hemp, Yarn & Cordage Co. (Hind-ley's Case) [1896] 2 Ch. 121; and other cases in the note preceding.

136 Rutland & Burlington R. Co. v. Lincoln, 29 Vt. 206.

137 See Perkins v. Savage, 15 Wend. (N. Y.) 412; Troy & Boston R. Co. v. Warren, 18 Barb. (N. Y.) 310; State v. Lehre, 7 Rich. Law (S. C.) 234.

138 See Appeal of Rowley, 115 Pa. St. 150.

138 Davidson v. Grange, 4 Grant Ch. (Can.) 377; McComb v. Frink, 149 U. S. 629; Burr v. Wilcox, 22 N. Y. 551; Stover v. Flock, 30 N. Y. 64, 41 Barb. (N. Y.) 162; Colt v. Clapp, 127 Mass. 476.

140 Stover v. Flock, 30 N. Y. 64. And see Orr v. Bigelow, 14 N. Y.

141 National Commercial Bank v. McDonnell, 92 Ala. 387; Union rule where a person assumes to subscribe for a person who is not capable of making a binding subscription.142

In other states it has been held that he does not become a stockholder, and is not liable on the subscription, because of his want of authority, but that the only remedy of the corporation is by an action against him to recover any damages it may have sustained by reason of his false assumption of authority.143-144

(c) Subscriptions by partners.—A partner may enter into a contract of subscription in the name of the firm, so as to bind the firm, if he is expressly authorized to do so by the other members of the firm, or without express authority, if the contract is within the scope of the business of the partnership, 145 but not otherwise. 146 A partner who subscribes for the firm without authority is himself liable unless his act is ratified by the other partners.147

### § 450. Authority and duties of persons receiving subscriptions.

(a) In general.—It is clear that a subscription to the stock of

Hotel Co. v. Hersee, 79 N. Y. 454, pany, and takes part of the stock 35 Am. Rep. 536; State v. Smith, 48 Vt. 266; Thompson v. Reno Savings Bank, 19 Nev. 103; Allibone v. Hager, 46 Pa. St. 48; Johnston v. Allis, 71 Conn. 207.

A subscription for stock signed by a person in his own name, "to be paid for by" another, renders the former liable as a subscriber. Langford v. Ottumwa Water Power Co., 59 Iowa, 283.

As to the liability of one who subscribes as "trustee" for the proposed corporation, see Johnston v. Allis, 71 Conn. 207; supra, note 123.

A person is liable on a subscription made by him in his wife's name, and entitled to the stock, where he intends it for himself, participates in organizing the com- N. Y. 454.

in his own name. See Shields v. Casey, 155 Pa. St. 253, 35 Am. St. Rep. 879.

142 See the cases in the note pre-

143 Salem Mill-Dam Corp. v. Ropes, 9 Pick. (Mass.) 187, 19 Am. Dec. 363.

144 See Mechem, Agency, § 541 et

145 Union Hotel Co. v. Hersee, 79 N. Y. 454; Maltby v. North Western Virginia R. Co., 16 Md. 422.

146 Patty v. Hillsboro Roller Mill Co., 4 Tex. Civ. App. 224; Morse v. Hagenah, 68 Wis. 603; Livingston v. Pittsburgh & Steubenville R. Co., 2 Grant Cas. (Pa.) 219.

147 Union Hotel Co. v. Hersee, 79

a corporation is not binding upon it, in the absence of ratification, unless the person accepting the same had authority from the corporation, or by reason of some provision in its charter or the general law under which it was organized. And it is equally clear, since mutuality of obligation is necessary,148 that a subscriber is not bound unless the corporation is bound. 149 Unless prevented, however, by the charter or general law, a corporation or its board of directors may authorize any person it may see fit to solicit and receive subscriptions. 150 If the charter or statute appoints particular persons, and expressly or impliedly makes their authority exclusive, subscriptions cannot be received by any other person, except in so far as the person so appointed may act by agent or deputy. The same is true where the articles of association appoint a particular person to receive subscriptions. It has been held, therefore, in some jurisdictions, that where the charter or statute appoints commissioners to open books and receive subscriptions, subscriptions not made through them are void.151

If subscriptions are received by a person who is without authority from the corporation, his act may be expressly or impliedly ratified by the corporation, so as to make the subscription binding to the same extent as if there had been previous authority;152 and there is a ratification if the corpora-

148 Ante, § 440.

149 Essex Turnpike Corp. v. Col- Rich. Law (S. C.) 278. lins, 8 Mass. 292; Deboe v. Wilson, 11 Ky. Law Rep. 581; Parker v. Northern Central Michigan R. Co., 33 Mich. 23; Kelsey v. Northern Light Oil Co., 45 N. Y. 505.

Where a corporation, at its first meeting, passed a vote authorizing a person to solicit and receive subscriptions, it was held that a subscription paper bearing date the same day must be considered

Eastern R. Co. v. Rodrigues, 10

v. 151 Shurtz Schoolcraft Three Rivers R. Co., 9 Mich. 269; Parker v. Northern Central Michigan R. Co., 33 Mich. 23; Northern Central Michigan R. Co. v. Eslow, 40 Mich. 222. Contra, North Eastern R. Co. v. Rodrigues, 10 Rich. Law (S. C.) 278. And see ante, § 445(e).

152 Taggart v. Western Maryland as authorized by the corporation, R. Co., 24 Md. 563, 89 Am. Dec. 760; no other subscription paper being Scarlett v. Academy of Music of proved to exist. South Bay Mea-Baltimore City, 46 Md. 132; Walkdow Dam Co. v. Gray. 30 Me. 547. er v. Mobile & Ohio R. Co., 34 Miss. 150 Lohman v. New York & Erie 245; Jefferson v. Hewitt, 103 Cal. R. Co., 2 Sandf. (N. Y.) 39; North 624. tion accepts the subscription, or otherwise recognizes it as binding. 153

Agents appointed to receive subscriptions have such authority only as is conferred upon them. As a rule, they have no authority to receive conditional subscriptions or subscriptions upon special terms, and if they do so, the corporation is not bound unless it ratifies their act.<sup>154</sup> The authority of an agent appointed to receive subscriptions is exhausted when subscriptions are received. The subscription at once inures to the benefit of the corporation, creating a contract between it and the subscriber, and the agent has no authority to modify or rescind the same.<sup>155</sup>

(b) Commissioners to open books and receive subscriptions.— Commissioners are sometimes appointed by the charter of a corporation or the general law under which it is organized to open subscription books and receive subscriptions. Or they may be appointed by the articles of association adopted in pursuance of the statute. As we have seen, the authority thus conferred may be exclusive, so that subscriptions cannot be received by others. The commissioners, however, may act by deputy, in so far as their duties are merely ministerial. The act of the commissioners in receiving subscriptions is ministerial where they are not required to exercise any discretion as to who shall be permitted to subscribe, and they may therefore, in such a case, appoint an agent or deputy to receive subscriptions, or ratify subscriptions received without authority

Compare East New York & Jamaica R. Co. v. Lighthall, 6 Rob. (N. Y.) 407, 36 How. Pr. 481, 5 Abb. Pr. (N. S.) 458.

The directors, however, have authority to receive conditional subscriptions and subscriptions on special terms, if the conditions or terms are not contrary to law or fraudulent as to other subscribers

155 Lowe v. Edgefield & K. R. Co., 1 Head (Tenn.) 659.

157 Supra, this section, (a).

<sup>153</sup> Taggart v. Western Maryland R. Co., 24 Md. 563, 89 Am. Dec. 760. 154 Farmers & Mechanics Bank v. Nelson, 12 Md. 35.

or creditors. McMillan v. Maysville & Lexington R. Co., 15 B. Mon. (Ky.) 218, 61 Am. Dec. 181. See post, §§ 455, 465, et seq.

commissioners to the corporation of subscriptions received by them is not necessary to render the subscribers liable to the corporation. Danbury & Norwalk R. Co. v. Wilson, 22 Conn. 435.

by a person assuming to act as their agent or deputy. 158 Commissioners cannot act by deputy in the performance, of acts in which they are required to exercise a discretion, for as to these they act judicially.159

The statutes sometimes require the commissioners to take an oath, but it has been held that their failure to do so will not render subscriptions received by them invalid.160

-Authority and powers of commissioners.-Since the commissioners appointed by a statute to open books and receive subscriptions are agents appointed by law, with special powers only, all persons who deal with them must look to the statute for their authority, and the corporation is not bound by any acts or contracts on their part which are beyond the authority conferred upon them by the statute. 161 The commissioners cannot bind the corporation without its consent by stipulations or conditions which are not within the scope of their author-But the corporation may ratify unauthorized stipulations or conditions, if they are within the powers conferred upon it by its charter, and not contrary to law. will be treated at length in subsequent sections. 163

Whether or not the commissioners have any discretion as to receiving subscriptions must depend upon the nature of the powers and duties conferred or imposed upon them by the They can undoubtedly refuse to receive fictitious subscriptions, or subscriptions by infants or others under a legal

159 Crocker v. Crane, 21 Wend. (N. Y.) 211, 34 Am. Dec. 228.

As to the distribution of stock in the case of excessive subscriptions, see post, § 512 et seq.

160 Hollman v. Williamsport & H. Turnpike Co., 9 Gill & J. (Md.)

161 Nippenose Mfg. Co. v. Stadon, 68 Pa. St. 256.

162 Nippenose Mfg. Co. v. Stadon, et seq.

158 Crocker v. Crane, 21 Wend. 68 Pa. St. 256; Pittsburg & Steu-(N. Y.) 211, 34 Am. Dec. 228; benville R. Co. v. Woodrow, 3 Saugatuck Bridge Co. v. Town of Westport, 39 Conn. 337. Phila. (Pa.) 271; Bavington v. Pittsburgh & Steubenville R. Co., 34 Pa. St. 358; Pittsburgh & Steubenville R. Co. v. Biggar, 34 Pa. St. 455; Bedford R. Co. v. Bowser, 48 Pa. St. 29; Caley v. Philadelphia & Chester County R. Co., 80 Pa. St. 363; McCarty v. Selinsgrove & North Branch R. Co., 87 Pa. St, 332; Boyd v. Peach Bottom Ry. Co., 90 Pa. St. 169. And see post, § 457(b).

163 See post, §§ 455 et seq., 465

disability, or by insolvent persons, or subscriptions which are conditional or upon special terms. And their discretionary power may extend even further.164

-Requirement of notice.-A statute authorizing the formation of a corporation, and appointing commissioners to open books and receive subscriptions for stock, generally, if not always, requires that public notice shall be given of the time and place of opening the books and receiving subscriptions. 165 Even when the statute does not in express terms require such notice, it is impliedly required where the time and place for opening the books and receiving subscriptions is not fixed by the statute, but is to be fixed by the commissioners. 166 object in requiring notice, however, is merely to prevent a monopoly of the stock by a few, and to give the public generally an opportunity to subscribe, and it has been held, therefore, that one who has subscribed cannot avoid liability on his subscription on the ground that the notice was not given. 167

Termination of commissioners' authority and responsibility. -When commissioners are appointed to open books and receive subscriptions for the purpose of organizing a corporation, their authority, duties, and responsibility continue un-

sioners, having discretionary power in receiving subscriptions, may limit the number of shares which any one individual shall be allowed to subscribe for. Brower v. Passenger Ry. Co., 3 Phila. (Pa.) 161, where a resolution was adopted that no commissioner or other person should have the privilege of subscribing for more than two hundred shares on the first day: Thomas v. Citizens' Passenger Ry. Co., 15 Leg. Int. (Pa.) 189, where their refusal to accept a subscription for more than half the stock by one person was sustained.

Commissioners appointed to receive stock subscriptions are not bound to receive a subscription by one signing as trustee, without disclosing the person for whom he 122, 9 Am. Dec. 495.

164 It has been held that commis- is acting. Thomas v. Citizens' Passenger Ry. Co., 15 Leg. Int. (Pa.) 189.

> As to the powers and duties of the commissioners where there is an oversubscription, see post, § 512 et seq.

> 165 A provision in the charter of a corporation that books for subscriptions shall be opened under the direction of the persons named in the act, and public notice thereof given, does not make it necessary that such notice shall be signed by all the persons named in the act. Penobscot R. Co. v. White, 41 Me. 512, 66 Am. Dec. 257.

166 State v. Bull, 16 Conn. 179.

167 Hager's Town Turnpike Road Co. v. Creeger, 5 Har. & J. (Md.) til the requisite amount of stock has been subscribed, and they have fulfilled all duties in relation to the organization of the corporation which are imposed upon them by the statute. 168 Their authority ceases, however, in the absence of special provision to the contrary, as soon as the required amount of stock is subscribed, the corporation organized, and its officers elected. The corporation then succeeds to the powers previously vested in the commissioners, and may sell or otherwise dispose of remaining shares of stock, without regard to conditions which may have been imposed upon the commissioners. 169 The commissioners no longer have any authority. 170 A bill will lie to enjoin the commissioners from acting further after the authority has so terminated. 171

-Subscriptions by commissioners or other agents.-When commissioners or other agents are appointed to open books or otherwise receive subscriptions to the stock of a corporation. they may enter their own names, and become subscribers, 172 provided they act fairly and without prejudice or fraud as to others who subscribe or apply to subscribe. But they cannot wrongfully exclude persons who wish to subscribe and subscribe for all the shares themselves. 178

168 Where commissioners are ap- Miss. 572; James v. Cincinnati, on a certain day, and keep them open until the required amount of ment, and the commissioners are filled in accordance with the statute. Lallande v. President & Directors of Louisiana State Ins. Co., has been called. Van Dyke v. 9 La. 326. Stout, 8 N. J. Eq. 333.

169 Taggart v. Western Maryland R. Co., 24 Md. 563, 89 Am. Dec. 760; Wellersburg & W. N. Plank Road Co. v. Hoffman, 9 Md. 568; Smith v. Bangs, 15 Ill. 399.

170 Smith v. Bangs, 15 Ill. 399; Ellison v. Mobile & Ohio R. Co., 36

pointed to open subscription books Hamilton & D. R. Co., 2 Disn. (Ohio) 261.

Commissioners appointed to restock is subscribed for, the time ceive subscriptions, and who are during which they are authorized directed by the statute to call a to keep the books open is unlim- meeting of stockholders to elect ited, except as to its commence- directors when a certain amount of stock has been subscribed, have not discharged from their duties no authority to open the books for as such until the subscription is further subscriptions after such amount has been subscribed, and the meeting of the stockholders

171 Smith v. Bangs, 15 Ill. 399.

172 Walker v. Devereaux, 4 Paige (N. Y.) 229; Greer v. Chartiers Ry. Co., 96 Pa. St. 391, 42 Am. Rep. 548. 173 See Attorney General v. Stev-

ens, 1 N. J. Eq. 369, 22 Am. Dec.

-- Neglect, fraud, or illegal action on the part of the commissioners.—If the commissioners appointed to open books and receive subscriptions neglect to proceed, or proceed illegally, mandamus will lie. 174 It has been held, however, that a writ of mandamus will not be granted to compel a particular commissioner to act, where his action is not necessary, as in a case where there are a number of other commissioners, who are willing to act, and the statute allows a majority to act. 175

If the commissioners fraudulently refuse to receive subscriptions from persons who have a right to subscribe, they are liable in damages, or, under some circumstances, the corporation may be liable. 176 But there is no such liability where the refusal to receive a subscription is due to an honest mistake. 177

If the commissioners fraudulently or wrongfully refuse to allow persons to subscribe, and attempt to subscribe for all the shares themselves, there can be no doubt of the power of a court of equity to control them, and to grant relief to a person or persons entitled and desiring to subscribe, for the commissioners are in the position of trustees. 178 If the commissioners fraudulently or wrongfully refuse to allow persons to subscribe, and take all the shares themselves, and then organize the corporation and enter upon the exercise of corporate powers under the charter, there is not a corporation de jure, and an information in the nature of quo warranto may be filed by the attorney general to oust it from the exercise of corporate pow-It has been held, however, that there is a corporation de facto, the existence of which cannot be collaterally attacked in a suit to enjoin it from exercising corporate powers, 180 and

<sup>174</sup> Walker v. Devereaux, 4 Paige (N. Y.) 229; In re White River 248.

Bank, 23 Vt. 478.

175 In re White River Bank, 23 ens, 1 N. J. Eq. 369, 22 Am. Dec.

<sup>176</sup> Lallande v. President & Directors of Louisiana State Ins. Co., 9 La. 326; Union Bank v. McDonough, 5 La. 66; Walden v. Union Bank, 6 La. 248.

<sup>177</sup> Walden v. Union Bank, 6 La.

<sup>179</sup> See Attorney General v. Stevens, 1 N. J. Eq. 369, 22 Am. Dec. 526. And see ante, § 93 et seq.

<sup>180</sup> See Attorney General v. Stevens, 1 N. J. Eq. 369, 22 Am. Dec.

that a court of equity has no jurisdiction to interfere by injunction either at the suit of an attorney general, or at the suit of individuals.181

Fraud practiced by one of the commissioners upon his cocommissioners in a matter as to which they act judicially does not affect the validity of their proceedings as respects subscribers, if they have jurisdiction in the premises. 182

### § 451. Revocation or withdrawal of subscriptions.

(a) Before formation of corporation or acceptance.—After a subscription has ripened into a binding contract, it is clear that it cannot be revoked by either party without the consent of the other. 183 But this is not true of mere offers to subscribe. Since a subscription to the stock of a corporation does not constitute a binding contract between the subscriber and the corporation until it has been accepted by the corporation, so as to be binding upon it, both because, until then, there is no agreement, and because, since there is no mutuality of obligation, there is no consideration, it necessarily follows, in the absence of a charter or statutory provision to the contrary, 184 that a subscription may be withdrawn at any time before it is accepted by the corporation, whether made before or after the formation of the corporation, just as any other offer may be withdrawn at any time before its acceptance.185

526. Compare, however, ante, § v. Whiting, 10 Mass. 327, 6 Am. 82(e). 181 Attorney General v. Stevens,

1 N. J. Eq. 369, 22 Am. Dec. 526. And see ante, §§ 98, 319.

183 See infra, this section, (b).

Dec. 124; Bryant's Pond Steam Mill Co. v. Felt, 87 Me. 234, 47 Am. St. Rep. 323; Carr v. Bartlett, 72 Me. 120; Starrett v. Rockland Fire 182 Crocker v. Crane, 21 Wend. & Marine Ins. Co., 65 Me. 374; (N. Y.) 211, 34 Am. Dec. 228. Wallace v. Townsend, 43 Ohio St. 537, 54 Am. Rep. 829; Plank's Tav-As to withdrawal by consent of ern Co. v. Burkhard, 87 Mich. 182; As to withdrawal by consent of the corporation, or release, see post, § 476.

184 See infra, this section, (e).

185 Hudson Real Estate Co. v. Green, 143 Pa. St. 256; Muncy Traction Engine Co. v. De La Rep. 434, 161 Mass. 10, 42 Am. St. Chittenden, 25 Fed. 544; Great Rep. 379; Essex Turnpike Corp. v. Western Telegraph Co. v. Loe-Rep. 379; Essex Turnpike Corp. v. wenthal, 154 Ill. 261; State v. Gar-Collins, 8 Mass. 292, as explained in Taunton & S. B. Turnpike Corp. field & K. R. Co., 1 Head (Tenn.) The fact that other subscribers have acted upon the strength of a subscription does not prevent its withdrawal before the corporation is formed and accepts the same.<sup>186</sup>

The application of this proposition where the corporation has not been formed is too clear to require more than its bare statement. "Until the organization of the corporation, the subscription is a mere proposition or offer, which may be withdrawn, like any other unaccepted offer. Unless the signer is bound upon a contract, he is not bound at all. It is open to him to \* \* \* For the time being, and until the corporation is organized, the writing does not take effect as a contract, because the contemplated party to the contract, on the other side, is not vet in existence; and for this reason, there being no contract, the whole undertaking is inchoate and incomplete, and since there is no contract the party may withdraw."187 "Such a subscription is not a completed contract. It takes two parties to make a contract. A nonexisting corporation can no more make a contract for the sale of its stock than an unbegotten child can make a contract for the purchase of it." 188

The application of the proposition to subscriptions after a corporation has been formed is equally clear. Until the corporation has become bound by an acceptance, there is no consideration for the subscription, and without a consideration, a promise is not binding. "A stock subscription is a transaction between the subscriber and the company, and the obligation of one can only be sustained by the corresponding obligation of the other. If both are not bound, neither is bound." 189

As we shall presently see, a statutory or charter provision may render subscriptions binding and irrevocable before the

<sup>659;</sup> Lewis v. Hillsboro Roller-Mill Co. (Tex. Civ. App.) 23 S. W. 338; Patty v. Hillsboro Roller Mill Co., 4 Tex. Civ. App. 224. And see the other cases cited ante, § 439.

<sup>186</sup> Hudson Real Estate Co. v. Tower, 161 Mass. 10, 42 Am. St. Rep. 379, 156 Mass. 82, 32 Am. St. Rep. 434.

<sup>&</sup>lt;sup>187</sup> Hudson Real Estate Co. v. Tower, 156 Mass. 82, 32 Am. St. Rep. 434.

<sup>&</sup>lt;sup>188</sup> Bryant's Pond Steam Mill Co. v. Felt, 87 Me. 234, 47 Am. St. Rep. 323.

<sup>&</sup>lt;sup>189</sup> Carlisle v. Saginaw Valley & St. Louis R. Co., 27 Mich. 315.

corporation is formed.<sup>190</sup> And a subscription under seal cannot be revoked if the corporation is in existence, unless the common-law doctrine that a seal renders a consideration unnecessary has been abolished.<sup>191</sup>

In a Minnesota case it was held that, where a number of persons sign a subscription paper agreeing to take stock in a corporation to be thereafter formed by them, there is (1) a contract between the subscribers themselves to become stockholders, without further act on their part, immediately upon the formation of the corporation, binding and irrevocable from the date of the subscription, unless canceled by consent of all the subscribers before acceptance by the corporation; and (2) a continuing offer to the proposed corporation, which, upon acceptance by it after its formation, becomes as to each subscriber a contract between him and the corporation; and that the promoter of the proposed corporation soliciting and obtaining subscriptions is the agent of the subscribers as a body to hold the subscriptions until the corporation is formed in accordance with the terms and conditions of the agreement, and then turn them over to it without any further act of delivery on the part of the subscribers, and therefore a delivery of the subscription to him is a complete delivery, so as to make it eo instanti a binding contract. 192

It seems very clear that there are several insuperable objections to this view. In the first place, it must be conceded that when a number of persons sign a subscription paper agreeing to take stock in a corporation to be formed, and expressly or impliedly agreeing to pay the amount of their subscriptions to the corporation when formed, they do not intend a contract with each other, but intend to contract with the corporation when formed, and the agreement must be construed by the courts in accordance with their intention. But even if there

<sup>190</sup> See infra, this section, (e). chine Co. v. Davis, 40 Minn. 110, 12
Am. St. Rep. 701.

<sup>191</sup> See infra, this section, (c).

Am. St. Rep. 701.

193 See Bryant's Pond Steam Mill

<sup>192</sup> Minneapolis Threshing Ma- Co. v. Felt, 87 Me. 234, 47 Am. St.

is a contract by each subscriber with the others, if one of the subscribers withdraws and repudiates this contract before the corporation is formed, there is merely a breach of this contract, and for such breach his only liability is to the other parties to the contract—the other subscribers—for the damages sustained by them by reason of his refusal to perform the contract.<sup>194</sup>

There cannot be a contract between each subscriber and the subscribers as a body, for until incorporation, the subscribers are not a body, but merely so many individuals.<sup>195</sup> Besides, to hold that there can be a contract between each subscriber and all the subscribers collectively, there being no incorporation as yet, is to hold that a person can contract with himself, whereas it is an elementary principle that a person cannot enter into a contract with himself, or with himself and others.<sup>196</sup>

The promoter of the proposed corporation cannot be said to be the agent of the corporation before it is formed, to receive and hold the subscriptions, for there can be no agency without an existing principal. Nor can the promoter be said to be the agent of the subscribers as a body to hold the subscriptions until the corporation is formed, and then turn them over to it, for a number of persons cannot be a body, or act as a body, or have an agent as a body, until they are incorporated. An unincorporated association is not a body, but merely a collection of individuals, and cannot be regarded in the law except as so many individuals. Therefore, if the promoter is the agent of the subscribers, he cannot be regarded otherwise than as the agent of each and every one of the subscribers as individuals. If he could be regarded as the agent of all the subscribers as a body, in receiving the subscriptions,

Rep. 323; and other cases in note 185, supra.

<sup>194</sup> Lake Ontario Shore R. Co. v. Curtiss, 80 N. Y. 219; Trustees of Phillips Limerick Academy v. Davis, 11 Mass. 113, 6 Am. Dec. 162.

<sup>&</sup>lt;sup>195</sup> Ante, §§ 17 et seq., 100, 101.

<sup>196</sup> Faulkner v. Lowe, 2 Exch. 595; Eastman v. Wright, 6 Pick. (Mass.) 316.

<sup>&</sup>lt;sup>197</sup> Ante, §§ 100, 101,

each subscriber would be delivering his subscription to his own agent, and therefore, in law, to himself.

It may be said that the promoter is, in receiving the subscription of each subscriber, the agent of all the others; but the result, at the most, is merely that there is a contract between each subscriber and all the others, and if he refuses to perform, his liability is to them for breach of his contract.

Assuming that there is both a contract by each subscriber with the other subscribers, and also a continuing offer by each subscriber to the corporation to be formed, the offer to the corporation can be withdrawn at any time before the corporation is formed and accepts the subscription, for until then, as between the subscriber and the proposed corporation, there is no mutuality or consideration, and therefore no contract. The agreement between the subscribers, if there be such an agreement, cannot supply the element of mutuality and consideration as between each subscriber and the corporation, and it cannot prevent revocation of the subscription regarded as an Such revocation is a breach of no offer to the corporation. contract with the corporation, for as yet there is no such con-If it is a breach of the contract between the subscribers, it is a breach for which they alone can sue. 198 As soon as the contract is thus broken by one of the subscribers, his liability and the rights of the other subscribers are fixed, and his subscription, as an offer to the proposed corporation, is no longer open for acceptance by the corporation when it is afterwards formed.

(b) After acceptance.—A subscription for stock cannot be revoked by the subscriber after it has been expressly or impliedly accepted by the corporation. There is then a binding contract, and neither party can withdraw without the consent of the other. And the same is true when a corporation makes an offer of shares by opening subscription books and soliciting subscriptions. When a person accepts the offer by entering his

<sup>198</sup> See Lake Ontario Shore R. Co. v. Curtiss, 80 N. Y. 219.

name as a subscriber, the contract of subscription is consummated, and neither the corporation nor the subscriber can withdraw. 199

In a Pennsylvania case, a railroad company, after its organization, opened subscription books and placed them in the hands of agents to receive subscriptions. One of these agents entered his own name in the book in his possession as a subscriber for a certain number of shares, but, after keeping the book for several months, he cut out his name for the purpose of withdrawing the subscription, because of some difference respecting pay for his services, and then returned it. held that he could not withdraw, as the contract of subscription was complete. The company, said the court, "made a continuing offer which became an agreement with each acceptant for the number of shares for which he subscribed. At the time a person signed his name, as a continuance of his act he might have erased it, as one who had written an acceptance of an offer by letter, before mailing the same might destroy it. But if the subscriber returned the book to the company's agent he could not afterwards withdraw his subscriptions, for he had completed the agreement. The defendant was acting as agent in soliciting subscriptions, no matter whether for pay or not, and by procuring subscriptions under his own name he declared his acceptance and admitted his agreement for the stipulated number of shares. The book was not his-he had no right to its possession but for a specific use. In that use he exhibited the evidence of his agreement with the company to every subsequent contracting party. Had the book been acci-

199 Greer v. Chartiers Ry. Co., 96
Pa. St. 391, 42 Am. Rep. 548; Cheraw & Chester R. Co. v. White, 10
County Park Ass'n, 68 Pa. St. 429;
S. C. 155; Gulf, Colorado & S. F.
Cravens v. Eagle Cotton Mills Co.,
R. Co. v. Neely, 64 Tex. 344; Athol
Music Hall Co. v. Carey, 116 Mass.
Bullock v. Falmouth & C. H. Turn-471; Ashuelot Boot & Shoe Co. v.
Hoit, 56 N. H. 548; International
Fair & Exposition Ass'n v. Walker,
Mich. 386; Richelieu Hotel Co.
V. International Military Encamp491; Lowe v. Edgefield & K. R.

dentally destroyed there was ample evidence of the contents of the written contract, upon which he could have held the company to performance; or if it refused, to payment of damages. Clearly the company was bound to him the same as to any other subscriber, and so was he to the company." 200

- (c) Subscriptions under seal.—A subscription under seal for stock in a corporation after it has been formed is binding before acceptance in those jurisdictions in which the commonlaw doctrine that a seal dispenses with the necessity for a consideration is still recognized.<sup>201</sup> But this is not true where the corporation has not been formed. In such a case, the subscription may be revoked at any time before the corporation is formed, notwithstanding it is under seal. "Until the organization of the corporation," said Judge Allen in a late Massachusetts case, "the subscription is a mere proposition or offer, which may be withdrawn, like any other unaccepted offer. Unless the signer is bound upon a contract, he is not bound at all. It is open to him to withdraw. It is not on the ground that there was no sufficient consideration; the seal would do away with any doubt on that score; but it is on the ground that for the time being, and until the corporation is organized, the writing does not take effect as a contract, because the contemplated party to the contract, on the other side, is not vet in existence; and for this reason, there being no contract, the whole undertaking is inchoate and incomplete, and since there is no contract, the party may withdraw." 202
- (d) Notice of revocation.—It is a general rule that revocation or withdrawal of an offer does not take effect, so as to prevent an acceptance thereof which will change it into a binding contract, until it is communicated to the person to whom the

Co., 1 Head (Tenn.) 659, and other cases cited under sections 439, 2 H. L. 296; Mansfield v. Hodgdon, 451(b).

<sup>200</sup> Greer v. Chartiers Rv. Co., 96 Pa. St. 391, 42 Am. Rep. 548. v. White, 10 S. C. 155.

201 See Xenos v. Wickham, L. R. 147 Mass. 304.

202 Hudson Real Estate Co. v. 96 Pa. St. 391, 42 Am. Rep. 548. Tower, 156 Mass. 82, 32 Am. St. See, also, Cheraw & Chester R. Co. Rep. 434, 161 Mass. 10, 42 Am. St. Rep. 379.

offer was made; and this rule necessarily applies to subscriptions for stock in a corporation. Until notice of its revocation or withdrawal is given, a subscription remains open for acceptance by the corporation.203

Notice of revocation or withdrawal need not be given to all the other subscribers. It is sufficient if it be given to the corporation, if in existence, or, if it is not, to the person who acted as promoter or agent in receiving it. A subscription to stock in a corporation may be withdrawn before its organization by notification of such withdrawal to another subscriber, who is acting as a member of the committee of subscribers appointed to manage their business, and who has been chosen their president.204

In England, as we have seen, when a written application is made for shares in a company, it is not binding until the company has accepted it, allotted the shares, and communicated such fact to the applicant, 205 and the application or offer may be revoked at any time before then.<sup>206</sup> Where the applicant expressly or impliedly authorizes the company to communicate notice of acceptance and allotment by mail, the acceptance is binding from the time the notice is properly deposited in the mail, and after that time there can be no revocation, even though the letter, without fault of the company, may be delayed in reaching the applicant or may be lost, and never reach In order that a revocation of the offer may be ef-

Co., 4 Ch. App. 527; In re Peruvian Ry.
Co., 4 Ch. App. 322; Harris' Case,
204 Hudson Real Estate Co. v. 7 Ch. App. 587; Household Fire &
Tower, 161 Mass. 10, 42 Am. St.
Rep. 379. See, also, Muncy Traction Engine Co. v. De La Green,
143 Pa. St. 269, where the notice of 143 Pa. St. 269, where the notice of re Brewery Assets Corp., [1894] 3 withdrawal was given to the chair-Ch. 272; Wilson's Case, 20 L. T. man of the meeting for the or-(N. S.) 962. ganization of the corporation.

In re Portuguese Consolidated Cop- 148.

203 Hudson Real Estate Co. v. per Mines, 42 Ch. Div. 160; Hebb's Tower, 161 Mass. 10, 42 Am. St. Case, L. R. 4 Eq. 9; Pellatt's Case, Rep. 379. And see ante, §§ 439, 2 Ch. App. 527; In re Peruvian Ry.

207 Household Fire & Carriage 205 Ante, § 439(b).

206 Ramsgate Victoria Hotel Co.

v. Montefiore, L. R. 1 Exch. 109; 587; Townsend's Case, L. R. 13 Fq. fectual, so as to prevent an acceptance, notice thereof must be communicated to the company. An acceptance and notice thereof before notice of a revocation will result in a binding contract.<sup>208</sup> When notice of a revocation is communicated by a letter deposited in the mail, the post office is the agent of the sender, not of the company, and the revocation does not take effect until the letter is actually received by the company. And since a letter of acceptance takes effect from the time it is properly mailed, it follows that a binding contract of subscription is made where a letter of acceptance is mailed after a letter revoking the application or offer is mailed, but before it has reached the company.<sup>209</sup>

(e) Subscriptions irrevocable by force of charter or statute.— It is undoubtedly within the power of the legislature to make subscriptions binding and irrevocable before the corporation is formed, or accepts the same. And it has been held, therefore, in several states, that the rule that a subscription to the stock of a corporation to be formed is not binding, and may be revoked by the subscriber at any time before the corporation is formed and accepts the same, does not apply to subscriptions made as a step authorized or required by a charter or general law in the formation of a corporation. Such a subscription, according to these decisions, although it cannot be regarded in any sense as a contract between the corporation and the subscriber, until the corporation is organized, is nevertheless binding upon the subscriber from the time it is made, by force of the statute, and cannot be withdrawn.<sup>210</sup> This view was taken by the court of appeals of New York under a general law authorizing the formation of railroad companies, and which provided for the opening of subscription books by commissioners,

<sup>208</sup> Harris' Case, 7 Ch. App. 587; Household Fire & Carriage Accident Ins. Co. v. Grant, 4 Exch. Div. 216.

<sup>209</sup> Harris' Case, 7 Ch. App. 587; Household Fire & Carriage Accident Ins. Co. v. Grant, 4 Exch. Div. 216.

210 Buffalo & New York City R. Co. v. Dudley, 14 N. Y. 336; Lake Ontario, Auburn & N. Y. R. Co. v. Mason, 16 N. Y. 451; Johnson v. Wabash & Mt. V. Plank-Road Co. 16 Ind. 389; Coppage v. Hutton, 124 Ind. 401; Greenbrier Industrial Exposition v. Rodes, 37 W. Va. 738.

and the taking of subscriptions, and payment of a deposit thereon, prior to the organization of a proposed company. held that subscriptions in compliance with the statute became binding, by force of the statute itself, from the time they were entered upon the subscription books, notwithstanding the fact that there could be no contract in the proper sense before organization of the corporation. Judge Selden said: rules of the common law, in regard to consideration and mutuality, do not apply to the case. Those rules may, I think, be regarded as superseded by the statute, which not only expressly authorizes subscriptions to be made in anticipation of the existence of the corporation, but impliedly, at least, recognizes their validity. Section 4 of the act by which the plaintiffs are incorporated provides, among other things, as follows: the said commissioners shall, at the time of any subscription, require the payment to them, by the person or persons subscribing, of five dollars towards and upon every hundred dollars so subscribed, and unless the same shall be paid the subscription shall be invalid.' This plainly implies that if the required payment is made the subscription shall be valid. But even without this clause it would, I think, be held that a statute which authorizes subscriptions in view of a subsequent incorporation, and regulates the manner in which they shall be made, must necessarily have the effect to give validity to such subscriptions, if made in accordance with the requirements of the act." 211

# § 452. Lapse of subscriptions.

As a subscription may be revoked by the subscriber at any time before it is accepted by the corporation, in the absence of a charter or statutory provision to the contrary, as explained in the preceding section, so, like other unaccepted offers, it may lapse. A subscription will lapse, or be revoked, as it is sometimes said, if the subscriber dies before it is accepted by the

211 Buffalo & New York City R. Co. v. Dudley, 14 N. Y. 336.

corporation, and it can make no difference whether there is notice of the death or not.<sup>212</sup> This is necessarily so, for "the continuance of an offer is in the nature of its constant repetition, which necessarily requires some one capable of making a repetition. Obviously this can no more be done by a dead man than a contract can, in the first instance, be made by a dead man." 213

A subscription will also lapse or be revoked if the subscriber becomes insane before it is accepted, if there is notice of the insanity, and perhaps without notice.214

The death or insanity of a subscriber does not revoke a subscription after it has been accepted by the corporation.<sup>215</sup>

A subscription will also lapse, and be no longer open for acceptance, if it is not accepted within the time, if any specified therein, or within a reasonable time, if no time is specified for acceptance. A corporation cannot wait indefinitely before accepting or rejecting a subscription. Nor can one be held indefinitely to his offer to take stock in a corporation to be formed 216

# § 453. Illegality in contracts of subscriptions.

A contract of subscription to the capital stock of a corporation, like other contracts, may be illegal, and therefore void, because it is in violation of some statutory prohibition, or of some principle of the common law, or because it is contrary to public policy. If a corporation is organized for a purpose which is prohibited by statute or by the common law, or which is contrary to public policy, subscriptions to the capital stock

<sup>212</sup> Pratt v. Trustees of Baptist Society of Elgin, 93 Ill. 475, 34 Am. Society of Elgin, 93 III. 475, 34 Am. Rep. 187; Phipps v. Jones, 20 Pa. St. 260, 59 Am. Dec. 708; Wallace v. Townsend, 43 Ohio St. 537, 54 Am. Rep. 829; Sedalia, Warsaw & S. Ry. Co. v. Wilkerson, 83 Mo. 235 Hudson Real Estate Co. v. Tower, 161 Mass. 10, 42 Am. St. Rep. 279 Rep. 379.

213 Pratt v. Trustees of Baptist

Society of Elgin, 93 III. 475, 34 Am. Rep. 187.

214 Beach v. First Methodist Episcopal Church, 96 Ill. 177.

215 See the cases above cited. And see supra, this section, (b).

216 Carter, Rittenberg & Hainlin Co. v. Hazzard, 65 Minn. 432; Knox v. Childersburg Land Co., 86 Ala.

are illegal and void, and can neither confer rights upon the subscribers nor be enforced by the corporation.<sup>217</sup> This is true, for example, of subscriptions for stock in a corporation formed for the purpose of carrying on an infringing telephone business;<sup>218</sup> and of subscriptions which are in violation of express charter, statutory, or constitutional prohibitions as to the terms or medium of payment.<sup>219</sup> Where a corporation attempts to increase its capital stock without legislative authority, subscriptions for the additional stock are void and unenforceable, both because they are without consideration, and because they are illegal.<sup>220</sup>

Illegality in the purpose of a corporation cannot be set up by subscribers for stock therein to defeat liability to creditors of the corporation, or to a receiver or an assignee in bankruptcy.<sup>221</sup>

## § 454. Proof of subscriptions.

The records of a corporation are competent and sufficient evidence to prove subscriptions to its capital stock, and to show whether or not the number of shares required by its charter have been subscribed, where no proof is introduced to destroy their effect.<sup>222</sup> If it is shown that a person's name appears on

<sup>217</sup> Clemshire v. Boone County Bank, 53 Ark. 512.

When a certificate of incorporation expresses no illegal purpose on the part of the corporators, and the agreements between the corporation and subscribers are valid on their face, subsequent corporate acts manifesting, or tending to show, an illegal purpose on the part of the directors,-as a purpose to combine in restraint of trade, or create a monopoly,-will not affect the legality of the corporation, so as to constitute a defense in actions by the corpora-tion on subscriptions. United States Vinegar Co. v. Foehrenbach, 148 N. Y. 58, affirming 74 Hun, 435. Compare United States Vinegar Co. v. 67 Hun, 356.

<sup>218</sup> Clemshire v. Boone County Bank, 53 Ark, 512.

<sup>219</sup> Knox v. Childersburg Land Co., 86 Ala. 180. And see ante, §§ 391, 395, 396.

<sup>220</sup> Ante, § 407(g).

<sup>221</sup> Cardwell v. Kelly, 95 Va. 570; Augir v. Ryan, 63 Minn. 373.

222 Penobscot R. Co. v. Dummer,
 40 Me. 172, 63 Am. Dec. 654; Penobscot R. Co. v. White,
 41 Me. 512, 66 Am. Dec. 257; Marlborough
 Branch R. Co. v. Arnold,
 9 Gray
 (Mass.) 159, 69 Am. Dec. 279.

Fense in actions by the corporation on subscriptions. United States Vinegar Co. v. Foehrenbach, 148 N. V. 58, affirming 74 Hun, 435. Compare United States Vinegar Co. v. Schlegel, 143 N. Y. 537, affirming 67 Hun, 356. the subscription or stock book of a corporation as a subscriber or stockholder, or upon the books of commissioners appointed to receive subscriptions, this is prima facie proof that he is a subscriber or stockholder.<sup>223</sup> The same is true where a subscription paper is produced, with a person's name thereon as a subscriber.224 If the original stock book has been lost, other books of record are admissible.<sup>225</sup> Mere declarations or reports by officers of a corporation are not admissible.<sup>226</sup> subscription be proved by a certificate or other paper, or a certified copy thereof, filed in the office of the secretary of state, where the filing of such paper is not required or authorized by any statute.227

Of course the books of record of a corporation, or a subscription paper, containing a person's name as a subscriber or stockholder, is nothing more than prima facie evidence, and may be rebutted by evidence that his name was placed there without his consent.228

ginia Real Estate Investment Co.,

96 Va. 177. 223 Turnbull v. Payson, 95 U. S. Where subscriptions are made 418; Hawley v. Upton, 102 U. S. by signing in a book, or on a slip 314; Glenn v. Liggett, 47 Fed. 472; of paper, and the subscriptions are Liggett v. Glenn, 4 U. S. App. 438, afterwards transcribed by an offi-51 Fed. 381; Glenn v. McAllister's cer of the corporation into a stock Ex'rs, 46 Fed. 883; President, etc., of Rockville & W. Turnpike Road v. Van Ness, 2 Cranch, C. C. 449, Fed. Cas. No. 11,986; South Branch Ry. Co. v. Long's Adm'r (Va.) 27 S. E. 297; Stuart v. Valley R. Co., 32 Grat. (Va.) 146; Pittsburgh, Wheeling & K. R. Co. v. Apple-gate, 21 W. Va. 172; Wood v. Coosa & Chattooga River R. Co., 32 Ga. 273; Lehman v. Glenn, 87 Ala. 618; Semple v. Glenn, 91 Ala. 245, 24 Am. St. Rep. 894; Congdon v. Win-sor, 17 R. I. 236; Glenn v. Orr, 96 N. C. 413; Hamilton & D. Plank Road Co. v. Rice, 7 Barb. (N. Y.) 157; Hoagland v. Bell, 36 Barb. (N. Y.) 57; Chapman v. Porter, 69 N. Y. 276; Marlborough Branch R. Co. v. Arnold, 9 Gray (Mass.) 159, And see ante, § 449.

the corporation, and who paid the 69 Am. Dec. 279; McHose v. Wheel-first assessment. Chapman v. Vir- ar, 45 Pa. St. 32; Iowa & Minnesota R. Co. v. Perkins, 28 Iowa, 281; Weber v. Fickey, 47 Md. 196.

book, it was held that the latter book was admissible in evidence, the officer being authorized by the subscribers to make the entries. Iowa & Minnesota R. Co. v. Perkins, 28 Iowa, 281.

224 Partridge v. Badger, 25 Barb.
(N. Y.) 146; Stuart v. Valley R.
Co., 32 Grat. (Va.) 146.

225 Congdon v. Winsor, 17 R. I.

A cash book entry of payment of an assessment has been held inadmissible. Glenn v. Liggett, Fed. 472.

226 Glenn v. Liggett, 47 Fed. 472. 227 See Troy & Rutland R. Co. v. Kerr, 17 Barb. (N. Y.) 581.

228 See the cases above cited.

Where subscriptions were made by signing the subscription books, or otherwise in writing, the books or writing are the best evidence, and unless they have been lost or destroyed, parol evidence is not admissible to prove the subscription.<sup>229</sup> they have been lost or destroyed, however, parol evidence is admissible.<sup>230</sup> And of course the testimony of an officer or agent of a corporation as to the fact, or other parol evidence, is admissible to prove a subscription which was not made in writing.231

In the absence of better evidence, as where there is no written subscription, declarations and admissions of a party are admissible to prove that he is a subscriber or stockholder. 232 Proof of conduct may also be admissible and sufficient, as proof that the party attended and participated in meetings of stockholders, acted as a director, paid assessments, etc.<sup>233</sup>

As we shall see, parol evidence is not admissible, in the absence of fraud or mistake, to vary or contradict a complete and unambiguous written contract of subscription.<sup>234</sup> Where, however, a subscription is ambiguous or incomplete on its face, parol evidence is admissible to explain it and supply omis-In the absence of fraud or mistake, an unambiguous written contract, which on its face is other than a subscription for stock in a corporation, cannot be varied by parol evidence for the purpose of showing that it was such a subscription.<sup>236</sup>

229 Graff v. Pittsburgh & Steubenville R. Co., 31 Pa. St. 489; 36 N. H. 545.
Pittsburgh & Steubenville R. Co. v. Gazzam, 32 Pa. St. 340; Taussig v. Glenn (C. C. A.) 51 Fed. 409; 232 Congdon v. Winsor, 17 R. I. Coffin v. Collins, 17 Me. 440.

subscription book has been lost, that the defendant authorized a share of stock to be issued to him, that a certificate was issued, that ler, 13 Metc. (Mass.) 311.

only stockholders were eligible to office, and that the defendant was elected and acted as president, and tery, 1 Walk. (Pa.) 40, where parol that he has made payments on his share, is clearly sufficient evidence of a subscription. York Park <sup>236</sup> Crane v. Elizabeth Library Building Ass'n v. Barnes, 39 Neb. Ass'n, 29 N. J. Law, 302.

233 Haynes v. Brown, 36 N. H. 230 Evidence that the original 545; York Park Building Ass'n v. Barnes, 39 Neb. 834; Barron v. Burrill, 86 Me. 66; Lexington & West Cambridge R. Co. v. Chand-

evidence was held admissible to show the name of the company.

Where commissioners are appointed by the legislature to open books and receive subscriptions for the purpose of organizing a corporation, and to certify the fact when the required amount of stock has been subscribed, their certificate, at least in the absence of a direct attack on the ground of fraud or collusion, is conclusive as to the validity of subscriptions received by them, and the amount thereof, so far as the legality of the organization of the corporation is concerned; and it cannot be shown, in contradiction of such a certificate, that less than the required amount of stock has been subscribed, or that some of the subscriptions are fictitious.<sup>237</sup>

- II. SUBSCRIPTIONS UPON EXPRESS CONDITIONS PRECEDENT, IMPLIED CONDITIONS PRECEDENT, AND CONDITIONAL DELIVERY OF SUBSCRIPTIONS.
- § 455. In general.—A subscription upon a condition precedent, or conditional subscription, is a subscription which, while it takes effect as a contract, and is irrevocable, as soon as it is accepted, does not make the subscriber a stockholder, or subject him to any liability, until performance of some condition, express or implied, unless the condition is waived by the subscriber, or he is estopped by his conduct to set up its nonperformance. In the absence of charter or statutory restrictions, conditional subscriptions may be made and accepted by a corporation after it is formed; but they cannot be made prior to the formation of the corporation, and counted in determining the amount of stock subscribed for the purpose of organization.

By the weight of authority, a written subscription may be delivered, even to the officers or agents of the corporation, with the understanding that it shall not take effect at all as a contract until the performance of an oral condition.

# § 456. Conditional subscriptions defined.

Subject to the limitations shown in the sections following, subscriptions to the capital stock of a corporation, instead of being

 <sup>&</sup>lt;sup>237</sup> Connecticut & Passumpsic field Bank v. Church, 29 Conn. 137;
 River R. Co. v. Bailey, 24 Vt. 465, Lane v. Brainerd, 30 Conn. 565.
 58 Am. Dec. 181. See, also, Litch-

absolute and unconditional, may be expressly made upon a condition or conditions precedent. And some conditions precedent, as we shall see, are implied when not expressed. A subscription upon a condition precedent, or conditional subscription, is a subscription which, by its express or implied terms, does not take effect so as to make the subscriber a stockholder, or confer or impose any rights or liabilities as a stockholder, until the performance or fulfillment of some condition, unless there is a waiver or an estoppel, but which does make him a stockholder, with all the rights and subject to all the liabilities arising out of such a relation, as soon as the condition is performed or fulfilled. Thus, as we shall see, a person may subscribe for stock in a railroad company upon condition that its road shall be located upon a certain route, which will render it beneficial to him. Until the road is so located, he does not become a stockholder, nor incur any liability to pay the amount of his subscription; but he does become a stockholder, and liable on his subscription, as soon as the road is so located.<sup>238</sup> Other illustrations will be found in the sections following.

# § 457. Conditional subscriptions distinguished from subscriptions upon special terms.

Conditional subscriptions, or subscriptions upon conditions precedent, must be distinguished from subscriptions upon special terms, which will be considered in subsequent sections. A conditional subscription, as we have seen, does not make the subscriber a stockholder, or render him liable to pay the amount of the subscription, until performance or fulfillment of the condi-A subscription upon special terms, on the other hand, is an absolute subscription, making the subscriber a stockholder, and rendering him liable as such, as soon as it is accepted; the

238 See Parker v. Thomas, 19 Ind. McMillan v. Maysville & Lexing-213, 81 Am. Dec. 385; Taggart v. ton R. Co., 15 B. Mon. (Ky.) 218, Western Maryland R. Co., 24 Md. 61 Am. Dec. 181; Cravens v. Eagle 563, 89 Am. Dec. 760; Webb v. Cotton Mills Co., 120 Ind. 6, 16 Am. Baltimore & Eastern Shore R. Co., St. Rep. 298; and other cases here-77 Md. 92, 39 Am. St. Rep. 396; inafter more specifically cited. special term being an independent stipulation, for a breach of which the subscriber's remedy is against the corporation for damages, 239 or else a stipulation affecting merely the mode or extent of payment, or the rights of the subscriber as a stockholder, etc.

Whether a subscription is conditional, or merely upon special terms, depends, of course, upon the intention of the parties, to be ascertained, as in other cases, by a construction of their contract. As was said in a Maine case, whether the conditions in a subscription are precedent or subsequent is a question of intent, to be determined by considering, not only the words of a particular clause, but also the language of the whole contract, the nature of the act, and the subject-matter to which it relates.<sup>240</sup> In case of doubt as to the intention of the parties, a subscription should be construed as an absolute subscription upon special terms, rather than as conditional.<sup>241</sup> The mere fact that the

239 Morrow v. Nashville Iron & Steel Co., 87 Tenn. 262, 10 Am. St. Rep. 658, 2 Keener's Cas. 989; Paducah & Memphis R. Co. v. Parks, 86 Tenn. 554; Red Wing Hotel Co. v. Friedrich, 26 Minn. 112; McGinnis v. Kortkamp, 24 Mo. App. 378; Johnson v. Georgia Midland & Gulf R. Co., 81 Ga. 725; Belfast & Moosehead Lake R. Co. v. Inhabitants of Brooks, 60 Me. 568; and cases cited in the notes following. See, also, post, § 465 et seq.

cases cited in the notes following. See, also, post, § 465 et seq. <sup>240</sup> Bucksport & Bangor R. Co. v. Inhabitants of Brewer, 67 Me. 295. See, also, Chamberlain v. Painesville & Hudson R. Co., 15 Ohio St. 225; Chase v. Sycamore & Courtland R. Co., 38 Ill. 215.

Where a subscription for stock in a corporation stipulated that the amount subscribed should not be payable until any contract which might be made by the company with another corporation for the purchase of its property should be ratified by the persons holding a majority of the stock, it was held that the making of a contract was not a condition precedent to liability on the subscription, and that

239 Morrow v. Nashville Iron & the subscription could not be withceel Co., 87 Tenn. 262, 10 Am. St. drawn, or its collection defeated, ep. 658, 2 Keener's Cas. 989; Paby assailing a contract actually cah & Memphis R. Co. v. Parks, is Tenn. 554; Red Wing Hotel Co. Cravens v. Eagle Cotton Mills Co., Friedrich, 26 Minn. 112; McGin- 120 Ind. 6, 16 Am. St. Rep. 298.

<sup>241</sup> Paducah & Memphis R. Co. v. Parks, 86 Tenn. 554; Morrow v. Nashville Iron & Steel Co., 87 Tenn. 262, 10 Am. St. Rep. 658, 2 Keener's Cas. 989; Swartwout v. Michigan Air Line R. Co., 24 Mich. 389; Chamberlain v. Painesville & Hudson R. Co., 15 Ohio St. 225.

In the case first cited it was said: "Conditional subscriptions to the stock of corporations are unusual, and often operate to defeat subscribers who become such absolutely and upon the faith that all the stock is equally bound to contribute to the hazards of the enterprise. It misleads creditors, and is the fruitful source of litigation and disaster. Tending to the ensnarement of creditors, and contrary to a sound public policy, conditional subscriptions to corporate shares ought not to be encouraged."

word "condition" is used, as where the subscription recites that it is made "upon condition that" a certain thing shall be done, does not make the provision a condition precedent.242

If it appears from the language of the subscription, or from extraneous circumstances, that it was intended that the subscriber should become and act as a stockholder prior to the performance of the stipulations contained in the contract, they are clearly special terms, and not conditions precedent, for a subscriber does not become a stockholder until conditions precedent are performed.<sup>243</sup> The same is true where it appears that the corporation was expected to expend money, which must be paid by the subscribers, before performance of the stipulation.<sup>244</sup> A stipulation in a subscription that the money paid thereon shall be applied by the corporation for a certain purpose clearly contemplates liability upon the subscription before performance of the stipulation, and the stipulation, therefore, is necessarily a special term, as distinguished from a condition.<sup>245</sup>

Illustrations.—Where it was provided in a subscription for stock in a railroad company that a certain percentage of the subscription should be paid when the road should be completed to the county line, and that the remainder should be paid in four equal installments of four months, as the work should progress through the county, "provided" the company should establish a depot at a specified point on the road, the court held that, while the provision as to the completion of the road to the county line was an express condition precedent, so that until then there was no liability to make the first payment, the provision as to establishing the depot was merely a special term, the performance of which was not necessary before enforcing

<sup>&</sup>lt;sup>243</sup> Morrow v. Nashville Iron & Steel Co., 87 Tenn. 262, 10 Am. St. Rep. 658, 669, 2 Keener's Cas. 989, 996; Lane v. Brainerd, 30 Conn. 565; Johnson v. Georgia Midland & Gulf R. Co., 81 Ga. 725.

<sup>242</sup> See Red Wing Hotel Co. v. v. Leavell, 16 B. Mon. (Ky.) 358; Friedrich, 26 Minn. 112. Red Wing Hotel Co. v. Friedrich, 26 Minn. 112; Connecticut & Passumpsic Rivers R. Co. v. Bailey, 24 Vt. 465, 58 Am. Dec. 181; Lane v. Brainerd, 30 Conn. 565; McGinnis v. Kortkamp, 24 Mo. App. 378. 245 Henderson & Nashville R. Co. v. Leavell, 16 B. Mon. (Ky.) 358, 244 Henderson & Nashville R. Co. and cases in the note preceding.

payment of the subscription.<sup>246</sup> A like construction has been placed upon provisions in subscriptions for stock in a railroad company that the road shall be located and constructed along a certain route, the location of the road being held a condition precedent, but its construction being a mere special term or condition subsequent; 247 upon a provision that the road shall be built through a certain town upon a line as run by the engineer, with a suitable depot for the convenience of the public: 248 or that the road is to be operated independently of a certain other railroad; 249 or that the subscriptions are to be expended between certain points on the road; 250 or that the company shall expend a certain amount of money in the construction of its road within a specified time, since "it would be exceedingly inconsistent to say that the corporation must expend that sum in the construction of their road, and at the same time deny them the right and power of collecting their subscriptions for that purpose."251

A provision in a subscription for stock in a hotel company that the hotel shall be located and built at a certain point is not

246 Paducah & Memphis R. Co. v. Parks, 86 Tenn. 554. See, also, Chamberlain v. Painesville & Hudson R. Co., 15 Ohio St. 225.

which the subscriber agrees to pay for the shares at such times and constructed" along a certain route, it does not mean that the road shall be actually constructed and v. Winkler, 29 Mo. 318. completed before any payment can be required, but means that, when the road is constructed and completed, it shall occupy the route designated. The subscription, therefore, becomes absolute and payable as soon as the road is definitely located along such route, and before it is constructed, and

struction. McMillan v. Maysville & Lexington R. Co., 15 B. Mon. (Ky.) 218, 61 Am. Dec. 181; Miller son R. Co., 15 Ohio St. 225.

247 Where a subscription for Co., 40 Pa. St. 237, 80 Am. Dec. stock in a railroad company, by 570; Chamberlain v. Painesville & Hudson R. Co., 15 Ohio St. 225; Swartwout v. Michigan Air Line places as may be required by the R. Co., 24 Mich. 389; Belfast & board of directors, is on condition Moosehead Lake R. Co. v. Moore, that the road shall be "located and 60 Me. 561; Bucksport & Bangor 60 Me. 561; Bucksport & Bangor R. Co. v. Inhabitants of Brewer. 67 Me. 295; North Missouri R. Co.

248 Belfast & Moosehead Lake R. Co. v. Inhabitants of Brooks, 60 Me. 568.

249 Johnson v. Georgia Midland & Gulf R. Co., 81 Ga. 725.

250 Lane v. Brainerd, 30 Conn.

<sup>251</sup> Connecticut & Passumpsic payments thereon can be then re-quired to raise funds for its con-58 Am. Dec. 181, 187. a condition precedent.<sup>252</sup> And the same is true of a stipulation in a subscription for organization stock in a corporation, that the corporation shall issue bonds to the subscriber to the full amount of his subscription, secured by a mortgage on its plant;253 and of a provision in the charter of a corporation that as soon as sufficient shares shall be subscribed, and sufficient money paid in, the trustees shall erect buildings required by the act.254

#### § 458. Validity of conditions precedent.

(a) Subscriptions after corporation is formed.—Conditional subscriptions to the stock of a corporation after it has been organized are valid, provided there is nothing in the charter or enabling act to prohibit them, and provided the conditions are not such as to render their performance beyond the powers of the corporation, or in violation of law, or contrary to public policv.255

rich, 26 Minn. 112.

258 Morrow v. Nashville Iron & Steel Co., 87 Tenn. 262, 10 Am. St. Rep. 658, 2 Keener's Cas. 989.

<sup>254</sup> Craig v. Cumberland Valley State Normal School, 72 Pa. St. 46. 255 McMillan v. Maysville & Lexington R. Co., 15 B. Mon. (Ky.) 218, 61 Am. Dec. 181; Taggart v. Western Maryland R. Co., 24 Md. western maryland R. Co., 24 Md. 563, 89 Am. Dec. 760; Baltimore & Drum Point R. Co. v. Pumphrey, 74 Md. 86; Clem v. Newcastle & Danville R. Co., 9 Ind. 488, 68 Am. Dec. 653; New Albany & Salem R. Co. v. McCormick, 10 Ind. 499, 71 Am. Dec. 337; Cravens v. Eagle Cotton Mills Co., 120 Ind. 6, 16 Am. St. Rep. 298; Burrows v. Smith, 10 N. Y. 550; Union Hotel Co. v. Hersee, 79 N. Y. 454, 35 Am. Rep. 536; Philadelphia & West Chester R. Co. v. Hickman, 28 Pa. St. 318; Pittsburgh & Connellsville R. Co. lowing.

v. Stewart, 41 Pa. St. 54; Caley v. A corporation may offer, allot, Philadelphia & Chester County R. and register shares to a person Co., 80 Pa. St. 363; Hanover Junction & Susquehanna R. Co. v. tle to the shares shall pass until

252 Red Wing Hotel Co. v. Fried- Grubb, 82 Pa. St. 36; Chamberlain v. Painesville & Hudson R. Co., 15 Ohio St. 225; Ashtabula & New Lisbon R. Co. v. Smith, 15 Ohio St. 328; Armstrong v. Karshner, 47 Ohio St. 276; Lesher v. Karshner, 47 Ohio St. 302; Chase v. Sycamore & Courtland R. Co., 38 III. more & Courtland R. Co., 38 Ill. 215; Brand v. Lawrenceville Branch R. Co., 77 Ga. 506; Hall v. Sims, 106 Ala. 561; Portland & Fairview R. Co. v. Spillman, 23 Or. 587; Burlington & Missouri River R. Co. v. Boestler, 15 Iowa, 555; Racine County Bank v. Ayres, 12 Wis. 512; Penobscot & Kennebec R. Co. v. Dunn, 39 Me. 587; Ticonic Water Power & Mfg. Co. v. Lang, 63 Me. 480; Bucksport & Bangor R. Co. v. Inhabitants of Brewer, 67 Me. 295; Shick v. Citizens' Enter-Me. 295; Shick v. Citizens' Enterprise Co., 15 Ind. App. 329, 57 Am. St. Rep. 230; and other cases more specifically cited in the notes fol-

By the weight of authority, in the absence of a charter or statutory prohibition, subscriptions for stock in an existing railroad company, or turnpike or plank road company, may be made upon the condition that the road shall be located, or both located and constructed, between certain points, or along a certain route, or that a depot shall be established at a certain point,<sup>256</sup> that the road shall be completed, or finished to a certain point,<sup>257</sup> or that work shall be commenced on the road, or commenced within a certain time,<sup>258</sup> or that the construction

he has fulfilled a certain condition, and may refuse to treat him as a stockholder until the condition has been fulfilled. Spitzel v. Chinese Corporation, 6 Manson, Bankr. Cas. 355, 80 Law T. (N. S.) 347.

<sup>256</sup> Taggart v. Western Maryland R. Co., 24 Md. 563, 89 Am. Dec. 760; Webb v. Baltimore & Eastern Shore R. Co., 77 Md. 92, 39 Am. St. Rep. 396; McMillan v. Maysville & Lexington R. Co., 15 B. Mon. (Ky.) 218, 61 Am. Dec. 181; Henderson & Nashville R. Co. v. Leavell, 16 B. Mon. (Ky.) 358; Bucksport & Bangor R. Co. v. Inhabitants of Brewer, 67 Me. 295; Connecticut & Passumpsic Rivers R. Co. v. Baxter, 32 Vt. 805; Wear v. Jacksonville & Savannah R. Co., 24 Ill. 593; New Albany & Salem R. Co. v. McCormick, 10 Ind. 499, 71 Am. Dec. 337; Shearer v. Evansville, I. & C. Straight Line R. Co., 12 Ind. 452; Parker v. Thomas, 19 Ind. 213, 81 Am. Dec. 385; North Missouri R. Co. v. Miller, 31 Mo. 19; Pacific R. Co. v. Seely, 45 Mo. 212, 100 Am. Dec. 369; Missouri Pacific Ry. Co. v. Tygard, 84 Mo. 264; Martin v. Pensacola & Georgia R. Co., 8 Fla. 370, 73 Am. Dec. 713; Miller v. Pittsburgh & Connellsville R. Co., 40 Pa. St. 237, 80 Am. Dec. 570; Cumberland Valley R. Co. v. Baab, 9 Watts (Pa.) 458, 36 Am. Dec. 132; Racine County Bank v. Ayres, 12 Wis. 512; Central Turnpike Corp. v. Valentine, 10 Pick. (Mass.) 142; County of Portage v. Wisconsin Central R. Co., 121 Mass. 460; Chapman v. Mad River & Lake Erie R. Co., 6 Ohio St. 119; Mans-

field, Coldwater & L. M. R. Co. v. Brown, 26 Ohio St. 223.

As to what constitutes location of a railroad, within the meaning of a condition, see Parker v. Thomas, 28 Ind. 277; Evansville, I. & C. Straight Line R. Co. v. Dunn, 17 Ind. 603.

It has been held in New York. contrary to the cases above cited. that a condition in a subscription for stock in a railroad company or turnpike company, that it shall locate its road along a certain route, is contrary to public policy and void, on the ground that it is against the interests of the general public that the directors, in locating the road, should be influenced by other motives or other considerations than the public good. Butternuts & Oxford Turnpike Co. v. North, 1 Hill (N. Y.) 518; Ft. Edward & Ft. Miller Plank Road Co. v. Payne, 15 N. Y. 583.

<sup>257</sup> Hall v. Sims, 106 Ala. 561; Toledo, Cincinnati & St. L. R. Co. v. Hinsdale, 45 Ohio St. 556.

Where notes given for subscriptions to stock in a railroad company are to become due and payable upon the decision of the directors that the road has been completed, publication of such decision in certain papers to be conclusive notice thereof, such decision and publication do not render the notes due and payable if the road has not in fact been completed. Garner v. Hall, 122 Ala. 221.

258 Taylor v. Fletcher, 15 Ind. 80.

of the road shall be put under contract within a certain time, with conditions in the contract that it shall be built within a certain time from the letting of the contract,259 or that certain grading work shall be actually done.260 or that a certain building of the corporation shall be erected.261 or that a contract with another corporation, which is under consideration, shall be ratified by a majority of the stockholders.262

A subscription may be made upon condition that the whole or a certain percentage of the capital stock shall be subscribed, or shall be subscribed by persons in a certain locality, or of a certain class.<sup>263</sup> Indeed, as we shall hereafter see, a condition that the full amount of the capital stock shall be subscribed is implied unless there is something in the contract of subscription, or in the charter, enabling act, or articles of association, to show an intention to the contrary.264

The effect of oral conditions is considered in a subsequent section.265

(b) Subscriptions before the corporation is formed.—In the preceding paragraph, we have been treating of subscriptions made after the creation of a corporation. Different rules apply, for obvious reasons, to subscriptions prior to and for the purpose of forming a corporation. According to the overwhelming weight of authority, when a special charter or general enabling act authorizing the formation of a corporation expressly or impliedly requires, as a condition precedent to incorporation or the exercise of corporate powers, that the entire anthorized capital stock, or a certain percentage thereof, shall

University, 35 Ill. 518.

Co., 120 Ind. 6, 16 Am. St. Rep. other cases cited post, § 505. 298; Brand v. Lawrenceville Branch R., 77 Ga. 506; People's Ferry Co.

<sup>265</sup> Post, § 460.

R. Co. v. Boestler, 15 Iowa, 555. Hench, 2 Walk. (Pa.) 478.

<sup>259</sup> Burlington & Missouri River v. Balch, 8 Gray (Mass.) 303; Troy Co. v. Boestler, 15 Iowa, 555. & Greenfield R. Co. v. Newton, 8 260 People's Freight Ry.Co. v.Gray (Mass.) 596; New York Excench, 2 Walk. (Pa.) 478.261 Johnston v.Ewing Female273; Union Hotel Co. v. Hersee, 79 niversity, 35 Ill. 518. N. Y. 454, 35 Am. Rep. 536; Phila-262 Cravens v. Eagle Cotton Mills delphia & West Chester R. Co. v. Co., 120 Ind. 6, 16 Am. St. Rep. Hickman, 28 Pa. St. 318; Shick v. 8. Citizens' Enterprise Co., 15 Ind. 268 Cravens v. Eagle Cotton Mills App. 329, 57 Am. St. Rep. 230; and

<sup>264</sup> See post, § 505 et seq.

be subscribed for, it contemplates and impliedly requires that the subscriptions shall be absolute and unconditional, and subscriptions cannot be made upon conditions precedent.266 reason for this doctrine is that the legislature, in requiring all or a certain part of the authorized capital stock to be subscribed before organization, or before the exercise of corporate powers, does so to protect the public against corporations which might otherwise undertake to do business and contract debts without the means of paying them. And it is held that conditional subscriptions are impliedly prohibited because the conditions may prevent their collection, and thus enable the corporation to commence business and contract debts without the required amount of capital.

In a leading case in the supreme court of the United States, where a statute authorizing the formation of a railroad company required that a certain per cent. of its capital stock should be subscribed before the corporation should exercise corporate powers, it was held that the statute impliedly required that subscriptions to the amount specified should be absolute and unconditional, and that conditional subscriptions were unauthorized. It was said in this case by Justice Strong: company is incorporated under general laws, the law prescribes that a certain amount of stock shall be subscribed before corporate power shall be exercised, if subscriptions, obtained before the organization was effected, may be sub-

Snediker, 18 Barb. (N. Y.) 317; Ft. Edward & Ft. Miller Plank Road Co. v. Payne, 15 N. Y. 583; In re Rochester, Hornellsville & L. R. Co., 50 Hun (N. Y.) 29; General Electric Co. v. Wightman, 3 App. Div. (N. Y.) 118; Caley v. Philadelphia & Chester County R. Bottom Ry. Co., 90 Pa. St. 169; fore any subscription for stock, Nippenose Mfg. Co. v. Stadon, 68 and one-half the authorized capi-

266 Burke v. Smith, 16 Wall. (U. Pa. St. 358; Pittsburgh & Steuben-S.) 390; Troy & Boston R. Co. v. ville R. Co. v. Biggar, 34 Pa. St. Tibbits, 18 Barb. (N. Y.) 297; Ma- 455; Bedford R. Co. v. Bowser, 48 cedon & Bristol Plank Road Co. v. Pa. St. 29; McCarty v. Selinsgrove & North Branch R. Co., 87 Pa. St.

> Compare, to the contrary, Chamberlain v. Painesville & Hudson R. Co., 15 Ohio St. 225.

Where the law under which a corporation was formed required articles of incorporation to be Co., 80 Pa. St. 363; Boyd v. Peach filed, and a charter obtained, be-Pa. St. 256; Bavington v. Pitts- tal stock to be subscribed before burgh & Steubenville R. Co., 34 organization, it was held that persequently rendered unavailable by conditions attached to them, the substantial requirements of the laws are defeated. purpose of such a requisition is, that the state may be assured of the successful prosecution of the work, and that creditors of the company may have, to the extent, at least, of the required subscription, the means of obtaining satisfaction of their claims. The grant of the franchise is, therefore, made dependent upon securing a specified amount of capital. If the subscriptions to the stock can be clogged with such conditions as to render it impossible to collect the fund which the state required to be provided before it would assent to the grant of corporate powers, a charter might be obtained without any available capital. Conditions attached to subscriptions, which, if valid, lessen the capital of the company, thus depriving the state of the security it exacted that the railroad would be built, and diminishing the means intended for the protection of creditors, are therefore a fraud upon the grantor of the franchise, and upon those who may become creditors of the corporation. They are also a fraud upon unconditional stockholders, who subscribed to the stock in the faith that capital sufficient would be obtained to complete the projected work, and who may be compelled to pay their subscriptions, though the enterprise has failed, and their whole investment has been lost. It is for these reasons that such conditions are denied any effect."267

Commissioners appointed to receive subscriptions prior to the organization of a corporation have no authority to receive conditional subscriptions. 268

In a Pennsylvania case, where a statute authorizing the

sons might subscribe conditionally, and that the conditions should not be held void, and the subscriptions held unconditional, for the purpose of determining whether the requisite amount of stock had been subscribed. Portland & Fair-

268 Bavington v. Pittsburgh & Steubenville R. Co., 34 Pa. St. 358; Pittsburgh & Steubenville R. Co. v. Biggar, 34 Pa. St. 455; Bedford R. Co. v. Bowser, 48 Pa. St. 29; Caley v. Philadelphia & Chester County R. Co., 80 Pa. St. 363; Mcview R. Co. v. Spillman, 23 Or. Carty v. Selinsgrove & North 587. Branch R. Co., 87 Pa. St. 332; 287 Burke v. Smith, 16 Wall. (U. Boyd v. Peach Bottom Ry. Co., 90 Pa. St. 169.

S.) 390.

formation of a railroad company required a certain per cent. of the capital stock to be subscribed as a condition precedent to organization, and appointed commissioners to receive subscriptions, etc., it was held that the commissioners had no authority to receive conditional subscriptions, and that such subscriptions, having been received, were to be treated as absolute. "The commissioners, who are appointed to receive such subscriptions," said the court, "are not the accredited agents of the corporation, for it is not yet in being, but are rather the agents of the public, acting under limited and definite powers, which every one is bound to know, and if he be misled by representations which such agents have no right to make, it is his own folly. Any other rule would lead to the procurement from the commonwealth of valuable charters without any absolute capital for their support, and thus give rise to a system of speculation and fraud which would be intolerable."269

The rule that conditional subscriptions prior to the formation of a corporation are invalid does not apply to subscriptions upon the condition that the whole or a certain percentage of the capital stock shall be subscribed for.<sup>270</sup> Indeed, as we shall hereafter see, such a condition is generally implied.<sup>271</sup>

# § 459. Effect of unauthorized conditional subscriptions.

If a corporation, after it has been formed, has no power under its charter or the enabling act to accept conditional subscriptions, such a subscription is not a binding contract at the time it is made, although accepted by the corporation. it is not an absolute nullity for all purposes. It is to be treated as an offer to take the stock upon performance of the conditions specified, which may be withdrawn, like any other offer, at any time before it is changed into a contract, but which, unless with-

ter County R. Co., 80 Pa. St. 363.

lute, while in New York they are

<sup>269</sup> Caley v. Philadelphia & Ches- regarded as absolutely void. See post, § 459.

<sup>271</sup> Post, § 505.

In Pennsylvania, unauthorized Gray (Mass.) 303; Montpelier & conditional subscriptions prior to incorporation are treated as absolute, while in New York they can

drawn, will continue open, and become binding as soon as the conditions are performed.272

With respect to subscriptions prior to the formation of a corporation, and which the commissioners or other persons receiving them have no authority to accept, it has been held in Pennsylvania that such a subscription is not void, but that the condition is void, as a fraud upon the public and upon unconditional subscribers, and that the subscription is to be treated as absolute and unconditional, both for the purpose of enforcing the same, and for the purpose of determining the amount of stock subscribed.<sup>273</sup> In New York and several other states, on the other hand, it has been held that the subscription itself is contrary to public policy and absolutely void for all purposes.<sup>274</sup>

#### § 460. Oral conditions affecting written subscriptions.

Whether or not oral conditions can be shown to qualify or affect a subscription in writing which is absolute on its face must be determined by the application of the general principles with respect to the admission of parol evidence to vary or add to the terms of a written contract. As to these principles, there

<sup>272</sup> Armstrong v. Karshner, 47 Ohio St. 276.

In Jefferson v. Hewitt, 103 Cal. 624, it was held that a note given in payment of a subscription for stock in a railroad company, conditioned upon completion of the road within a given time, in violation of a statutory prohibition against the issue of stock except for money paid, labor done, or property actually received, and for which a certificate of stock was issued, was without consideration and void, as the subscription and certificate were void, and that the condition could not be treated as void, and the subscription and note treated as absolute.

Caley v. Philadelphia & Chester County R. Co., 80 Pa. St. 363; Mc-Carty v. Selinsgrove & North Branch R. Co., 87 Pa. St. 332; Boyd v. Peach Bottom Ry. Co., 90 Pa. St. 169. See, also, Burke v. Smith. 16 Wall. (U. S.) 390; supra, § 458 (b). See Miller v. Hanover Junction & S. R. Co., 87 Pa. St. 95.

274 Troy & Boston R. Co. v. Tibbits, 18 Barb. (N. Y.) 297; Macedon & Bristol Plank Road Co. v. Snediker, 18 Barb. (N. Y.) 317; Ft. Edwards & Ft. Miller Plank Road Co. v. Payne, 15 N. Y. 583; In re Rochester, Hornellsville & L. R. Co., 50 Hun (N. Y.) 29; General Electric Co. v. Wightman, 3 App. treated as absolute.

278 Bavington v. Pittsburgh & C. Straight Line R. Co. v. Posey, Steubenville R. Co., 34 Pa. St. 358;
Pittsburgh & Steubenville R. Co. Gravel Road Co., 52 Ind. 51; La Pittsburgh & Steubenville R. Co. Gravel Road Co., 52 Ind. 51; La v. Biggar, 34 Pa. St. 455; Bedford Grange & Monticello Plank Road R. Co. v. Bowser, 48 Pa. St. 29; Co. v. Mays, 29 Mo. 64. is some difference of opinion. According to the weight of authority, parol evidence is not admissible to import conditions into a written contract which is absolute and unconditional on its face, unless failure to express the conditions was due to fraud or mistake; and this doctrine has been applied where it has been attempted to show by parol evidence that a written subscription to the stock of a corporation absolute on its face was in fact made upon conditions.275

In Pennsylvania the doctrine with respect to the admissibility of parol evidence is not the same as in other states. It is there held that if the subscription would not have been made except for the oral condition it may be proved, provided the rights of creditors are not involved, since to allow the corporation to enforce the subscription would operate as a fraud.<sup>276</sup>

By the weight of authority, in the absence of an estoppel, parol evidence is admissible to show that a written subscription was not to take effect as a contract at all until the performance of a condition, as it is admitted in such a case, not to vary the terms of the written instrument, but to show that there is no agreement at all.277

# § 461. Effect of valid conditional subscriptions.

(a) Before performance or fulfillment of condition.—A conditional subscription, as distinguished from a subscription upon

<sup>275</sup> Wight v. Shelby R. Co., 16 B. cannot be qualified or limited by Mon. (Ky.) 4, 63 Am. Dec. 522; proof of any general understand-North Carolina R. Co. v. Leach, 4 ing among the subscribers that the Jones (N. C.) 340; Masonic Temple Ass'n v. Channell, 43 Minn. 353; Miller v. Preston, 4 N. M. 396; Chattanooga, Rome & C.R.Co. v. Worthen, 98 Ga. 599; Anderson v. Middle & East Tennessee Central R. Co., 91 Tenn. 44; Ellison v. Mobile & Ohio R. Co., 36 Miss. 572; Braddock v. Philadelphia, Marlton & M. R. Co., 45 N. J. Law, 363; Corwith v. Culver, 69 Ill. 502; Brownlee v. Ohio, Indiana & Illinois R. Co., 18 Ind. 68. And see post, § 467(e).

Subscriptions which are absolute and unconditional on their face same should be abandoned and not collected unless a given amount should be subscribed. Hickling v. Wilson, 104 Ill. 54,

<sup>276</sup> See McCarty v. Selinsgrove & North Branch R. Co., 87 Pa. St. 332; Miller v. Hanover Junction & Susquehanna R. Co., 87 Pa. St. 95, 30 Am. Rep. 349; Caley v. Philadelphia & Chester County R. Co., 80 Pa. St. 363; Rinesmith v. People's Freight Ry. Co., 90 Pa. St. 262. Compare McClure v. People's Freight Ry. Co., 90 Pa. St. 269.

277 Post, § 464.

special terms,<sup>278</sup> assuming that the subscription and the condition are valid, neither confers any rights as a stockholder nor imposes any liability, until the condition is substantially performed,<sup>279</sup> unless performance is waived by the subscriber, or he is estopped by his conduct to set up its nonperformance.<sup>280</sup>

Revocation or withdrawal.—It has been held that a subscription for stock, by which the subscriber agrees to take the stock upon performance of a condition precedent by the corporation,—as upon the location of a railroad along a certain route, for example,—is merely a continuing offer to take the stock, which may be revoked or withdrawn at any time before the condition is performed, and which becomes binding only when it is accepted by the corporation by performing the condition.<sup>281</sup> And these decisions are undoubtedly sound if the corporation does not, when it first accepts the conditional subscription, bind itself to perform the condition. If performance on its part is entirely optional with it, there is no mutuality of obligation, and therefore no contract.

278 Ante, § 457. 279 Parker v. Thomas, 19 Ind. 213, 81 Am. Dec. 385; Shearer v. Am. Dec. 159; McMillan v. Maysville & Lexington R. Co., 15 B. Mon. (Ky.) 218, 61 Am. Dec. 181; Philadelphia & West Chester R. Co. v. Hickman, 28 Pa. St. 318; People's Freight Ry. Co. v. Hench, 2 Walk. (Pa.) 478; McCarty v. Selinsgrove & North Branch R. Co., 87 Pa. St. 332; Chase v. Sycamore & Courtland R. Co., 38 Ill. 215; Burlington & Missouri River R.
Co. v. Boestler, 15 Iowa, 555; PeR. Co., 24 Md. 563, 89 Am. Dec.
nobscot & Kennebec R. Co. v. 760; Webb v. Baltimore & Eastern Dunn, 39 Me. 587; Ticonic Water Shore R. Power & Mfg. Co. v. Lang, 63 Me. Rep. 396.

480; Bucksport & Bangor R. Co. v. Inhabitants of Brewer, 67 Me. 295; 213, 81 Am. Dec. 385; Shearer v. McCann v. American v. Evansville, I. & C. Straight Line Co., 4 Neb. 256; Livesey v. Omaha R. Co., 12 Ind. 452; Taylor v. Hotel Co., 5 Neb. 50; Hall v. Sims, Fletcher, 15 Ind. 80; Cravens v. 106 Ala. 561; Porter v. Raymond, Eagle Cotton Mills Co., 120 Ind. 6, 53 N. H. 519; Monadnock R. Co. v. 16 Am. St. Rep. 298; Martin v. Felt, 52 N. H. 379; Brewers' Fire Pensacola & Georgia R. Co., 8 Fla. Ins. Co. v. Burger, 10 Hun (N. Y.) 370, 73 Am. Dec. 713; Frankfort & 56; Trott v. Sarchett, 10 Ohio St. Shelbvville Turnpike Co. v. 241; Toledo, Cincinnati & St. L. R. Echols v. City of Bristol, 90 Va. 165; Branch v. Augusta Glass Works, 95 Ga. 573; Brown v. Dibble, 65 Mich. 520; Swartwout v. Michigan Air Line R. Co., 24 Mich. 389; Johnson v. Schar, 9 S. D. 536; and other cases cited ante, § 456 et seq. See, also, post, § 505.

280 See post, § 463.

Shore R. Co., 77 Md. 92, 39 Am. St.

This cannot apply, however, where the corporation binds itself to perform the condition, for then there is a contract consisting of mutual promises, in which each promise is a consideration for the other. It is a well-settled principle of the law of contracts, that a bilateral contract, under which the right to require performance by one of the parties is dependent upon the performance of a condition precedent by the other, is binding upon both parties as soon as it is made, and that the party whose promise is conditional, while he cannot be held liable to perform, or for failure to perform, until performance of the condition by the other, cannot withdraw before the time for such performance without the other's consent. There is no reason why this principle should not be applied to conditional contracts of subscription, in the absence of anything to show that the parties did not intend to make a binding contract, as distinguished from a mere revocable offer. Of course, if there is no consideration for the subscriber's promise, it is not binding, and the cases above cited would apply, and there is no consideration if the corporation does not bind itself to perform the condition, but has a mere option to do so. There is a consideration, however, if the corporation binds itself to perform the condition, so that the subscriber would have a right of action against it on its refusal or failure to do so. In an Ohio case, it was held that a subscription for stock in a railroad company upon a condition precedent became a binding contract as soon as it was accepted by the corporation; that the subscriber, while he could not be compelled to pay the amount of the subscription before performance of the condition, could not withdraw before expiration of the time for performance; and that, notwithstanding an attempted withdrawal, he became absolutely liable when the corporation performed the condition. 282

(b) After performance or fulfillment of condition.—A subscription upon a condition precedent becomes absolute as soon as

<sup>&</sup>lt;sup>282</sup> Armstrong v. Karshner, 47 Cravens v. Eagle Cotton Mills Co., Ohio St. 276. See, also, Hutchins 120 Ind. 6, 16 Am. St. Rep. 298. v. Smith, 46 Barb. (N. Y.) 235;

the condition is substantially performed, without any further act or consent upon the part either of the corporation or of the subscriber, both for the purpose of rendering the subscriber liable on the subscription, and for the purpose of constituting him a stockholder, with all the rights of a stockholder, as the right to vote at corporate meetings, the right to receive dividends, etc.<sup>283</sup>

(c) Construction and performance of conditions.—The same principles apply to the construction of conditional subscriptions as in the case of any other conditional contract. The conditions must be performed, unless they are waived or the subscriber is estopped; but all that is required is that they shall be substantially performed according to the intention of the parties. And in determining whether they have been performed, they must be reasonably construed.<sup>284</sup>

If a subscription is payable in installments, each installment being upon a separate and distinct condition, each installment becomes payable upon performance of its condition, without regard to the other conditions.<sup>285</sup>

Conditions precedent must be performed within the time, if any, prescribed by the contract. If they are not performed within such time, the subscriber is discharged, in the absence of a waiver or estoppel, and he cannot be rendered liable by a

283 McMillan v. Maysville & Lexington R. Co., 15 B. Mon. (Ky.) 218, 61 Am. Dec. 181; Taggart v. Western Maryland R. Co., 24 Md. 563, 89 Am. Dec. 760; Webb v. Baltimore & Eastern Shore R. Co., 77 Md. 92, 39 Am. St. Rep. 396; Cravens v. Eagle Cotton Mills Co., 120 Ind. 6, 16 Am. St. Rep. 298; North Missouri R. Co. v. Miller, 31 Mo. 19; Chamberlain v. Painesville & Hudson R. Co., 15 Ohio St. 225; Ashtabula & New Lisbon R. Co. v. Smith, 15 Ohio St. 328; Mansfield, Coldwater & L. M. R. Co. v. Brown, 26 Ohio St. 223; Mansfield, Coldwater & L. M. R. Co. v. Stout, 26 Ohio St. 241; Philadelphia & Delaware County R. Co. v. Conway, 177

288 McMillan v. Maysville & Lexgton R. Co., 15 B. Mon. (Ky.) Hersee, 79 N. Y. 454, 35 Am. Rep. 18, 61 Am. Dec. 181; Taggart v. 536; Pittsburgh & Connellsville R. 264 Co. v. Plummer, 37 Pa. St. 413; 275 Cornell's Appeal, 114 Pa. St. 153; 277 More & Eastern Shore R. Co., 77 278 d. 92, 39 Am. St. Rep. 396; Cra-279 cras v. Eagle Cotton Mills Co., 120 Graffenreid, 12 Rich. L. (S. C.) 277 Spartanburg & Union R. Co. v. December v. Eagle Cotton Mills Co., 120 Graffenreid, 12 Rich. L. (S. C.)

284 Union Hotel Co. v. Hersee, 79
N. Y. 454, 35 Am. Rep. 536; Hall
v. Sims, 106 Ala. 561; Cornell's Appeal, 114 Pa. St. 153; People's Ferry Co. v. Balch, 8 Gray (Mass.)
303; Jackson v. Stockbridge, 29
Tex. 394, 94 Am. Dec. 290.

<sup>285</sup> Coos Bay, R. & E. Railroad & Navigation Co. v. Dixon, 30 Or. 584.

subsequent performance.<sup>286</sup> If no time for performance is fixed by the subscription, conditions must be performed within what is a reasonable time under the circumstances of the particular case.287

(d) Notice of performance.—Notice of performance of a condition precedent in a subscription is necessary, of course, if it is required by the contract. There are some cases in which it has been held necessary without an express requirement, 288 but the better opinion is to the contrary, at least unless the fact of performance is peculiarly within the knowledge of the corporation. 289 The fact that a subscription provides that a certain kind of notice of performance of conditions precedent shall be sufficient does not make notice in the way mentioned necessary, but actual notice in any other way is sufficient. 290

Notice may be inferred or presumed from the circumstances. Thus, notice to a subscriber for stock in a railroad company that the road was located in a certain place, as required by the subscription, was presumed, where the place was a city of only fifteen thousand inhabitants, and the subscriber resided there, and the road had been constructed and was in operation for several years before he was sued on his subscription. 291

When the first installment on a subscription for stock is not to become due until a certain amount of stock is subscribed, a

<sup>286</sup> Ticonic Water Power & Mfg. Brown, 80 Iowa, 277; Hutchins v. o. v. Lang, 63 Me. 480; Morris Smith, 46 Barb. (N. Y.) 235. Co. v. Lang, 63 Me. 480; Morris Canal & Banking Co. v. Nathan, 2 Hall (N. Y.) 262; Bohn Mfg. Co. v. land R. Co., 38 Ill. 215; Trott v. Lewis, 45 Minn. 164; Freeman v. Sarchett, 10 Ohio St. 241. Matlock, 67 Ind. 99; Burlington & Co. v. Tygard, 84 Mo. 264, where (Iowa) 42. time was held not to be of the es-. sence of the contract.

<sup>287</sup> Ticonic Water Power & Mfg. Co. v. Lang, 63 Me. 480; Stevens v. McCormick, 10 Ind. 499, 71 Am. v. Corbitt, 33 Mich. 458; Blake v. Dec. 337.

288 Chase v. Sycamore & Court-

289 Spartanburg & Union R. Co. Missouri River R. Co. v. Boestler, v. De Graffenreid, 12 Rich. L. (S. 15 Iowa, 555; Memphis, Kansas & C.) 675, 78 Am. Dec. 476; Nichols C. Ry. Co. v. Thompson, 24 Kan. v. Burlington & Louisa County 170. But see Missouri Pacific Ry. Plank Road Co., 4 G. Greene

290 New Albany & Salem R. Co. v. McCormick, 10 Ind. 499, 71 Am. Dec. 337.

291 New Albany & Salem R. Co.

call for the first installment operates as notice to subscribers that the required amount has been subscribed.292

### Implied conditions precedent.

In the preceding sections, we have been dealing with subscriptions upon express conditions precedent. It remains to consider implied conditions. Although a subscription may be absolute and unconditional on its face, certain conditions precedent are implied as a matter of law.

(a) Fixing amount of capital stock.—By the weight of authority, when the capital stock of a corporation is not fixed by its charter, it must be fixed by the stockholders or directors before any stockholder can be held liable on his subscription.<sup>293</sup> It need not be done, however, in any particular manner. Any act on the part of the directors which has the effect of fixing the amount of stock for the time being is sufficient.294

2 Hall (N. Y.) 504.

293 Somerset & Kennebec R. Co. v. Cushing, 45 Me. 524; Somerset R. Co. v. Clarke, 61 Me. 379; Pike v. Bangor & Calais Shore Line R. Co., 68 Me. 445; Worcester & Nashua R. Co. v. Hinds, 8 Cush. (Mass.) 110; Lexington & West Cambridge R. Co. v. Chandler, 13 Metc. (Mass.) 311; Troy & Greenfield R. Co. v. Newton, 8 Gray (Mass.) 596.

Compare City Hotel v. Dickinson, 6 Gray (Mass.) 686; Ward v. Griswoldville Mfg. Co., 16 Conn. 593; Kirksey v. Florida & Georgia Plank Road Co., 7 Fla. 23, 68 Am. Dec. 426; Warwick R. Co. v. Cady, 11 R. I. 131.

But where the charter of a corporation limited the capital stock to not less than 500 nor more than \$100 each, and authorized the directors to assess upon 500 shares as soon as subscribed for, and limit, all the shares to be equally Buck, 65 Me. 536.

202 Harlem Canal Co. v. Seixas, assessed, it was held not to be necessary for the corporation to determine and fix the ultimate amount of its capital stock within the maximum limit before making assessments upon the first 500 shares subscribed. White Mountain R. Co. v. Eastman, 34 N. H.

294 Where, by an act underwhich a corporation was formed, its capital stock was not to exceed 2,000 shares, the number to be determined from time to time by the directors, and assessments on each share were not to exceed \$100, and the directors caused subscription books to be opened, and, after more than 250 shares were subscribed for, voted to close the books, but passed no other vote fixing the number of shares, it was held that the vote in effect lawfully fixed the number of shares for 10,000 shares of the par value of the time being at the number subscribed for, so as to render assessments thereon valid. Lexington & West Cambridge R. Co. v. Chandfrom time to time to enlarge the ler, 13 Metc. (Mass.) 311. See, alcapital stock up to the maximum so, Bucksport & Bangor R. Co. v.

- (b) Subscription of entire capital stock, or of a certain percent-' age thereof.—As we shall see at length in a subsequent section. it is an implied condition precedent to liability as a subscription, unless there is something to show a contrary intention, that the full amount of capital stock, or particular percentage thereof, fixed by the charter, enabling act, articles of association, contract of subscription, or by the directors or stockholders when they are given authority to settle the same, shall be subscribed in good faith and by competent persons. And until this condition is fulfilled, the corporation cannot levy assessments or otherwise enforce subscriptions, in the absence of a waiver or estoppel.<sup>295</sup>
  - (c) Payments on subscriptions.—Payments on subscriptions are clearly not conditions precedent to liability thereon for the full amount, unless it is expressly so provided by the charter or enabling act, or by the contracts of subscription themselves. Even when the charter or enabling act expressly requires a certain percentage of subscriptions to be paid at the time of subscribing, or before commencement of business, the requirement is not to be construed as making such payments conditions precedent to liability on subscriptions, unless such an intention clearly appears.296
  - (d) Issue or tender of certificate or stock.—As was shown in a former chapter, a certificate is merely evidence of the holder's ownership of stock, and is not at all necessary to make one a stockholder.297 And it is well settled that the issue or tender of a certificate of stock is not a condition precedent to the right of a corporation to levy assessments or maintain an action on a subscription for stock, 298 unless it is expressly required by the

<sup>295</sup> Post, § 503 et seg.

<sup>296</sup> See post, § 508 et seq.

<sup>297</sup> Ante, § 378.

<sup>298</sup> Chester Glass Co. v. Dewey, 16 Mass. 94, 8 Am. Dec. 128; Brigham v. Mead, 10 Allen (Mass.)

Mitchell v. Beckman, 64 Cal. 117; California Southern Hotel Co. v. Callender, 94 Cal. 120, 28 Am. St. Rep. 99; Pacific Fruit Co. v. Coon, 107 Cal. 447; Heaston v. Cincinnati & Ft. Wayne R. Co., 16 Ind. 275, 79 Am. Dec. 430; New Albany & 245; Spear v. Crawford, 14 Wend. 79 Am. Dec. 430; New Albany & (N. Y.) 20, 28 Am. Dec. 513; Rut-Salem R. Co. v. McCormick, 10 Ind. ter v. Kilpatrick, 63 N. Y. 604; 499, 71 Am. Dec. 337; Vawter v. Chaffin v. Cummings, 37 Me. 76; Ohio & Mississippi R. Co., 14 Ind.

contract of subscription.<sup>299</sup> A different rule applies to a sale of stock, as distinguished from a subscription. In such a case, issue or tender of a certificate is a condition precedent to the right to maintain an action for the price. 300

Even in the case of a subscription for stock, as distinguished from a sale of stock, the corporation, before it can require payment, must be ready and willing to deliver the stock subscribed for, and this must be alleged, and proved if denied.\*

174; Drover v. Evans, 59 Ind. 454; Slipher v. Earhart, 83 Ind. 173; Chandler v. Northern Cross R. Co., 18 Ill. 190; Wemple v. St. Louis, Jerseyville & S. R. Co., 120 Ill. 196; Delaware R. Co. v. Tharp, 1 Houst. (Del.) 149; Fulgam v. Macon & Brunswick R. Co., 44 Ga. 597; South Georgia & Florida R. Co. v. Ayres, 56 Ga. 230; Webb v. Baltimore & Eastern Shore R. Co., 77 Md. 92, 39 Am. St. Rep. 396; Astoria & South Coast Ry. Co. v. Hill, 20 Or. 177; Paducah & Memphis R. Co. v. Parks, 86 Tenn. 554; Columbia Electric Co. v. Dixon, 46 Minn. 463; Marson v. Deither, 49 Minn. 423; Minneapolis Harvester Works v. Libby, 24 Minn. 327; Walter A. Wood Harvester Co. v. Robbins, 56 Minn. 48; Shelbyville Trustees v. Shelbyville & Eminence Turnpike Co., 1 Metc. (Ky.) 54; Smith v. Gower, 2 Duv. (Ky.) 17; Buffington v. Butler & Kittaning Turnpike Road Co., 3 Pen. & W. (Pa.) 71; Sinkler v. Indiana & Ebensburg Turnpike Road Co., 3 Pen. & W. (Pa.) 149; Corwith v. Culver, 69 Ill. 502; Wheeler v. Millar, 90 N. Y. 353; Kohlmetz v. Calkins, 16 App. Div. (N. Y.) 518; Walter A. Wood Harvester Co. v. Walter A. Wood Harvester Co. v. Jefferson, 71 Minn. 367; Schaeffer v. Missouri Home Ins. Co., 46 Mo. 248.

It has been held necessary, however, to allege a readiness and willtingness to deliver a proper certifiind. 220; Burrows v. Smith, 10 N.
cate. James v. Cincinnati, Hamilton & D. R. Co., 2 Disn. (Ohio) & C. R. Co., 104 Ga. 13; Knoxville,
261; Walter A. Wood Harvester Cumberland Gap & L. R. Co. v.
Co. v. Jefferson, 57 Minn. 456. See, City of Knoxville, 98 Tenn. 1. also, ante, § 378(b).

299 Courtright v. Deeds, 37 Iowa, 503; Cooper v. McKee, 49 Iowa, 286; Lawrence v. Smith, 50 Iowa, 703; Hedge v. Gibson, 58 Iowa, 656. See Marson v. Deither, 49 Minn. 423; Paducah & Memphis R. Co. v. Parks, 86 Tenn. 554.

A provision in a contract of subscription that "certificates of stock issue to said subscribers as to other stockholders in said company, upon the payment of their sub-scription," was held not to make delivery or tender of a certificate a condition precedent. Paducah & Memphis R. Co. v. Parks, 86 Tenn. 554. Compare, however, Courtright v. Deeds, 37 Iowa, 503, and other Iowa cases, supra.

300 Fulgam v. Macon & Brunswick R. Co., 44 Ga. 597; Marson v. Deither, 49 Minn. 423.

\* James v. Cincinnati, Hamilton & D. R. Co., 2 Disn. (Ohio) 261; Walter A. Wood Harvester Co. v. Jefferson, 71 Minn. 367; St. Louis Rawhide Co. v. Hill, 72 Mo. App. 142; Knoxville, Cumberland Gap & L. R. Co. v. City of Knoxville, 98 Tenn. 1; Lehigh v. Chattanooga, Rome & C. R. Co., 104 Ga. 13.

There can be no recovery on a subscription, if valid certificates for the entire authorized capital stock have already been issued. James v. Cincinnati, Hamilton & D. R. Co., 2 Disn. (Ohio) 261; McCord v. Ohio & Mississippi R. Co., 13 Ind. 220; Burrows v. Smith, 10 N.

Of course, a subscriber cannot be

- (e) Formation of the corporation, and effect of irregularity or failure to incorporate.—In the nature of things, before there can be any contract of subscription at all, there must be in existence a corporation capable of contracting and suing, or there must be an estoppel to deny that there is such a corporation. It is not always necessary, however, that there shall be a corporation de jure, as distinguished from a corporation de facto. Nor, if there is an estoppel, is it necessary that there shall be even a corporation de facto.
- Subscriptions after formation of corporation.—As we have seen in a former chapter, a corporation de facto has the same capacity to contract, and to enforce its contracts, as a corporation de jure. 301 And this doctrine applies to subscriptions to the capital stock of a corporation after its organization and assumption of corporate powers. If a person, therefore, subscribes for stock in a corporation after its organization and assumption of corporate powers, it is sufficient to show a de facto corporate existence to support an action on the subscription. cannot be defeated by showing that there have been such irregularities in the organization of the corporation that there is not a corporation de jure. 302

Further than this, although there may not be even a corporation de facto, a subscription may be enforceable by reason of the doctrine of estoppel. As we have seen, it is a general rule, recognized in most jurisdictions, although not in all, that a per-

ed for. A subscriber for the common stock of a corporation, therefore, cannot be compelled to receive preferred stock instead. Knoxville, Cumberland Gap & L. R. Co. v. City of Knoxville, 98 Tenn. 1.

801 As to what is necessary to constitute a corporation de facto, and the effect of contracts with such a corporation, see ante. §§ 80-

compelled to accept something dif-ferent from what he has subscrib- er's Cas. 1937, 1 Cum. Cas. 975; Buffalo & Allegheny R. Co. v. Cary, 26 N. Y. 75, 1 Smith's Cas. 89, 1 Cum. Cas. 411; Cayuga Lake R. Co. v. Kyle, 64 N. Y. 185; Tar River Navigation Co. v. Neal, 3 Hawks Navigation Co. v. Neal, 3 Hawks (N. C.) 520; Duke v. Cahawba Navigation Co., 10 Ala. 82, 44 Am. Dec. 472; Hamilton v. Clarion, Mahoning & P. R. Co., 144 Pa. St. 34; Ogden Clay Co. v. Harvey, 9 Utah, 497; Swartwout v. Michigan Air Line R. Co., 24 Mich. 389; Monroe v. Ft. Wayne L. & P. Co. 28 302 Heaston v. Cincinnati & Ft. v. Ft. Wayne, J. & S. R. Co., 28 Wayne R. Co., 16 Ind. 275, 79 Am. Mich. 272; Spartanburg & Ashe-Dec. 430, 1 Cum. Cas. 417; Eaton ville R. Co., 14 S. C. 281.

son who enters into a contract with an association as a corporation thereby admits its corporate existence, and is estopped to deny the same, whether it be a corporation de facto or not, in any action or proceeding based upon or arising out of the con-In those jurisdictions in which this doctrine is recognized, a person who subscribes for stock in an association as an existing corporation is estopped to deny its corporate existence for the purpose of escaping liability on the subscription, both as against creditors and as against the corporation itself.304

A subscriber is estopped in all jurisdictions as against creditors, where he has acted as an officer or stockholder, or otherwise participated in holding out the corporation as having a legal existence.305

Subscriptions before corporation is formed.—The principles above stated do not apply to the full extent when a subscription for stock is made prior to the formation of a corporation, and in contemplation thereof. In such a case, it is a condition precedent to any liability upon the subscription, implied if not expressed, that the corporation shall be legally organized as contemplated; and the subscriber, therefore, may defeat an action on his subscription, unless estopped, by showing that the condition has not been performed. There must be, in the absence of an estoppel, not merely a corporation de facto, but a corporation de jure. 306 As we shall hereafter see, however, a subscriber may be estopped in such a case.307

there cited.

305 Post, § 515. 306 Indianapolis Furnace & Mining Co. v. Herkimer, 46 Ind. 142, 1 Smith's Cas. 97, 1 Cum. Cas. 970; Rikhoff v. Brown's Rotary Shuttle Sewing Machine Co., 68 Ind. 388; Dorris v. Sweeney, 60 N. Y. 463; Crocker v. Crane, 21 Wend. (N. Y.) 211, 34 Am. Dec. 228; Capps v. Hastings Prospecting Co., 40 Neb. it was held that, where such agree-470, 42 Am. St. Rep. 677; Richment was not acknowledged prior mond Factory Ass'n v. Clarke, 61 to the issue of the certificate of

303 As to this doctrine, and the Me. 351; Greenbrier Industrial Exconflict of authority on particular position v. Rodes, 37 W. Va. 738; points, see ante, § 83 et seq. Schloss v. Montgomery Trade Co., 
 804 See post, § 515, and cases 87 Ala. 414. 13 Am. St. Rep. 51;

 ere cited.
 Coppage v. Hutton, 124 Ind. 401;
 Williams v. Citizens' Enterprise Co., 153 Ind. 496; Id., 25 Ind. App. 351. Compare Cayuga Lake R. Co. v. Kyle, 64 N. Y. 185.

Under the West Virginia statute, providing that an agreement for the formation of a corporation "shall be acknowledged by the several corporators before a justice,"

To render a subscription prior to incorporation binding, the corporation which is formed must be the corporation contemplated by the subscriber, for if an offer is made to take stock in a particular corporation to be formed, another and different corporation cannot accept the same. In such a case, no agreement at all is formed.<sup>308</sup>

Organization of corporation after creation.—When a corporation is created by a special act or under a general law, so that it has acquired corporate existence, but organization is necessary before it can enter upon the transaction of business, the organization must be effected before any action can be maintained on subscriptions for stock.<sup>309</sup> But subscriptions are not rendered invalid by the fact that they were received before organization, or before the election of directors. <sup>310</sup>

Noncompliance with conditions subsequent.—As we shall hereafter see, failure of a corporation to comply with conditions subsequent <sup>311</sup> in the charter or enabling act, as conditions precedent to the right to do business, so that the state might proceed against it to forfeit its charter, cannot be set up by a subscriber to escape liability on his subscription.<sup>312</sup>

Cure of defects in organization by legislature.—A defect in the organization of a corporation may be cured by a subsequent curative act of the legislature, or by an act recognizing the corporation as having a legal existence, and in such a case persons who subscribed for stock prior to such act cannot afterwards set up the defect in the organization of the corporation to escape liability on their subscriptions.<sup>313</sup>

incorporation, the company did not obtain corporate existence as to those who, by such preliminary agreement, subscribed stock, and that they were not liable on such subscription. Greenbrier Industrial Exposition v. Rodes, 37 W. Va. 312 See 312 See

307 Post, § 515.

308 Ante, § 439 (d).

309 Carlisle v. Cahawba & Marion R. Co., 4 Ala. 70.

310 Covington, C. C. & J. Plank Road Co. v. Moore, 3 Ind. 510; Lackey v. Richmond & Lancaster Turnpike Road Co., 17 B. Mon. (Ky.) 43.

311 See ante, § 73.

312 See post, § 488.

313 Illinois Grand Trunk R. Co. v. Cook, 29 Ill. 237; Cayuga Lake R. Co. v. Kyle, 5 Thomp. & C. (N. Y.) 659, 64 N. Y. 185. See ante, § 77.

# § 463. Waiver of conditions by subscriber, and estoppel.

When a person makes a contract to pay money or perform any other act upon the performance of a condition precedent, he may expressly or impliedly waive the performance of the condition at any time, and thereby render his promise absolute. once waived the condition, he cannot afterwards insist upon its performance, or claim a discharge by reason of its nonperformance. This principle applies with full force to subscriptions to the stock of a corporation.314

A waiver of a condition precedent may be implied from any act on the part of the subscriber, with knowledge that the condition has not been performed, which is inconsistent with an intention to insist upon performance of the condition, and it will always be implied, as a matter of law, and irrespective of the actual intention, from any act, with such knowledge, which the subscriber could not lawfully do if he intended to insist upon. the condition.315 A waiver will generally be implied, for example, if a subscriber takes part in stockholders' meetings, or otherwise acts as a stockholder, before the condition is performed, for a conditional subscription does not make the subscriber a stockholder until performance of the condition.316

Conn. 565; Hutchins v. Smith, 46 Barb. (N. Y.) 235; Graves v. Sa-line County, 161 U. S. 359; Lee v. Imbrie, 13 Or. 510; Hanover Juncv. Jefferson (Minn.) 74 N. W. 149; Co. v. Boestler, 15 Iowa, 555; Des Y.) 235. Moines Valley R. Co. v. Graff, 27

314 Keller v. Johnson, 11 Ind. Co. v. Johnson, 30 N. H. 390, 64 337, 71 Am. Dec. 355; O'Donald v. Am. Dec. 300; McAllister v. In-Evansville, I. & C. Straight Line dianapolis & Cincinnati R. Co., 15 R. Co., 14 Ind. 259; Slipher v. Ear- Ind. 11; Parks v. Evansville, I. & hart, 83 Ind. 173; Chamberlain v. C. Straight Line R. Co., 23 Ind. Painesville & Hudson R. Co., 15 567; Seymour v. Jefferson (Minn.) Ohio St. 225; Lane v. Brainerd, 30 74 N. W. 149; and other cases 74 N. W. 149; and other cases cited in the notes following.

A subscriber waives a condition that a certain amount of stock shall be subscribed by making tion & Susquehanna R. Co. v. contracts and incurring liabilities Grubb, 82 Pa. St. 36; Cornell's on behalf of the corporation, with Appeal, 114 Pa. St. 153; Seymour knowledge that the required amount has not been subscribed. Burlington & Missouri River R. Hutchins v. Smith, 46 Barb. (N.

316 McAllister v. Indianapolis & Iowa, 99, 1 Am. Rep. 256; Mont-pelier & Wells River R. Co. v. ton & Cincinnati R. Co., 15 Ind. 11; Day-pelier & Wells River R. Co. v. ton & Cincinnati R. Co. v. Hatch, Langdon, 45 Vt. 137. Langdon, 45 Vt. 137.

1 Disn. (Ohio) 84; New Hamps

15 Lane v. Brainerd, 30 Conn. shire Central R. Co. v. Johnson,

165; New Hampshire Central R. 30 N. H. 390, 64 Am. Dec. 300; There is also a waiver of conditions in a subscription where the subscriber acts as a director or other officer of the corporation, when his right to do so depends upon his being a stockholder.317

Payment of a subscription, or of a part thereof, with knowledge of nonperformance of a condition precedent to liability to make the payment, will be held a waiver of the condition, unless there is something to show that a waiver was not intended.318 But part payment will not constitute a waiver, if it appears from the circumstances or otherwise that there was no such intention.319 Giving an absolute note in payment of a conditional subscription is a waiver 320 unless the circumstances are such as to show that the parties did not so intend. In the latter case,

Lane v. Brainerd, 30 Conn. 565; Pittsburgh & Steubenville R. Co. v. Proudfit, 2 Pittsb. R. (Pa.) 85. Compare Ridgefield & New York R. Co. v. Reynolds, 46 Conn. 375, where it was held that a subscriber to stock in a railroad company on condition that no more than a two per cent, assessment should be made until the sum estimated to be necessary to build the road should be subscribed did not waive the condition by soliciting other subscriptions, taking part in meetings of stockholders, accepting office as a director, and taking part in directors' meetings, or by being present at meetings at which the making of construction contracts was announced and assessments voted, it not appearing that he took part in such meeting.

Merely being present at a meeting as a spectator, without taking any part therein, does not show a waiver of conditions precedent. New Hampshire Central R. Co. v. Johnson, 30 N. H. 390, 64 Am. Dec. 300.

317 Lane v. Brainerd, 30 Conn. 565; Dayton & Cincinnati R. Co. v. Hatch, 1 Disn. (Ohio) 84. Compare Ridgefield & New York R. Co. v. Reynolds, 46 Conn. 375.

Dayton & Cincinnati R. Co. v. Hatch, 1 Disn. (Ohio) 84; Union Hotel Co. v. Hersee, 79 N. Y. 454, 35 Am. Rep. 536.

A person who subscribes conditionally for stock of a railroad company, the subscription being payable in land, waives the condition by making an absolute conveyance of the land to the company, and receiving his Parks v. Evansville, I. Straight Line R. Co., 23 Ind. 567.

319 Pittsburgh & Connellsville R. Co. v. Stewart, 41 Pa. St. 54; Johnson v. Schar, 9 S. D. 536; Jewett v. Lawrenceburgh & Upper Mississippi R. Co., 10 Ind. 539; Parker v. Thomas, 19 Ind. 213, 81 Am. Dec. 385; Atlantic Cotton Mills v. Abbott, 9 Cush. (Mass.) 423.

820 Keller v. Johnson, 11 Ind. 337, 71 Am. Dec. 355; O'Donald v. Evansville, I. & C. Straight Line R. Co., 14 Ind. 259; Evansville, f. & C. Straight Line R. Co. v. Dunn, 17 Ind. 603; Slipher v. Earhart, 83 Ind. 173.

Giving a note for the balance of conditional subscription, and taking a receipt from the company stipulating that the amount of the note, when paid, shall be applied 318 Cornell's Appeal, 114 Pa. St. on the stock, is prima facie a 153; Mack's Appeal (Pa.) 7 Atl. waiver of the condition. Cham-481; Parks & Evansville, I. & C. berlain v. Painesville & Hudson Straight Line R. Co., 23 Ind. 567; R. Co., 15 Ohio St. 225.

there is no waiver.<sup>321</sup> Of course, a condition precedent upon which a subscription has been made may be expressly waived by agreement or stipulation, either in writing or oral; and it is waived by subsequently entering into an agreement or stipulation which is inconsistent with performance of the condition, whether the condition is expressly referred to or not.322

Acts of a subscriber which would otherwise constitute a waiver of conditions will not have this effect if he does not know at the time that the conditions have not been performed, but supposes that they have. Thus, a stockholder who subscribes on condition that a certain amount of stock shall be taken, and who, without knowledge that the required amount has not been subscribed, waives notice of a stockholders' meeting, and votes by proxy at a special meeting, does not thereby waive performance of the condition.323

Estoppel.—Aside from any question of intentional waiver, a subscriber may be estopped by his conduct from saving that his subscription was conditional. 324 Where a commissioner appoint-

stock in a railroad company was made on condition that the road should be located over a certain route, and notes for the subscription were given, payable at such times as the installments fell due. it was held that the fact that the notes were unconditional did not make the giving of them a waiver of the right to have the road located as stipulated before being called upon to pay the notes. Parker v. Thomas. 19 Ind. 213, 81 Am. Dec. 385.

A note given by a subscriber in payment of his subscription, on the false representation by an agent of the corporation that a condition precedent has been complied with, is not a waiver, and may be avoided for the fraud. Taylor v. Fletcher, 15 Ind. 80.

Co., 15 Ky. Law Rep. 782; Hanover Junction & Susquehanna R. lis Threshing Machine Co. v. Da-Co. v. Grubb, 82 Pa. St. 36; Montvis, 40 Minn. 110, 12 Am. St. Rep. pelier & Wells River R. Co. v. 701 (post, § 464).

321 Where a subscription for Langdon, 45 Vt. 137: Henderson & Nashville R. Co. v. Moss, 2 Duv. (Ky.) 242.

> 323 Portland & Fairview R. Co. v. Spillman, 23 Or. 587; Denny Hotel Co. v. Gilmore, 6 Wash. 152; Birge v. Browning, 11 Wash. 249; Hawkins v. Citizens' Real Estate & Investment Co. (Or.) 64 Pac.

> The same is true of a part payment in ignorance of nonperformance of the condition. Johnson v. Schar, 9 S. D. 536; Hawkins v. Citizens' Real Estate & Investment Co. (Or.) 64 Pac. 320.

> 324 Bavington v. Pittsburgh & Steubenville R. Co., 34 Pa. St. 358; New Hampshire Central R. Co. v. Johnson, 30 N. H. 390, 64 Am. Dec.

As to estoppel to set up that a 322 Hall v. Owensboro Wagon subscription was delivered subject to an oral condition, see Minneapoed to receive subscriptions recites, in the certificate showing that the requisite number of shares have been subscribed to entitle the company to incorporation, that he has personally subscribed for a number of shares, he is estopped to afterwards set up that his subscriptions were conditional. 325 And where a subscription is upon an express or implied condition that the full amount of stock, or a certain percentage thereof, shall be subscribed, the subscriber will be estopped from setting up nonperformance of the condition, if, with knowledge of its nonperformance, he has participated in stockholders' meetings, and in votes for expending money and making contracts, or in other acts which could not be properly done except upon the assumption that the subscribers intended to proceed before performance of the condi-The fact that a subscriber was present at a meeting of stockholders does not estop him from insisting upon performance of conditions precedent, or claiming a discharge because of nonperformance, where he was merely a spectator, and took no part in the meeting, and all his acts showed an intention not to pay his subscription. 327

### § 464. Conditional delivery of subscriptions.

It is a settled general principle in most jurisdictions,—although the doctrine has been criticised as "founded more on refinement of logic than upon sound practical grounds,"<sup>328</sup> and repudiated altogether in some jurisdictions, <sup>329</sup>—that it may be shown that a written agreement, including contracts of subscription, was delivered with the understanding that it should not take effect until the performance or fulfillment of an oral condition, even though the delivery may have been to an agent or even a director of the corporation, the evidence being admitted in such a case, not for the purpose of adding a condition to

<sup>325</sup> Bavington v. Pittsburgh & Co. v. Johnson, 30 N. H. 390, 64 Steubenville R. Co., 34 Pa. St. 358, Am. Dec. 300.

<sup>326</sup> New Hampshire Central R. 328 Minneapolis Threshing Ma-Co. v. Johnson, 30 N. H. 390, 64 chine Co. v. Davis, 40 Minn. 110, Am. Dec. 300. And see post, § 507. 12 Am. St. Rep. 701.

<sup>327</sup> New Hampshire Central R. 329 See infra, this section.

the contract or agreement, but for the purpose of showing that as yet there has been no contract or agreement at all.330

This doctrine, however, is to be applied only in "cases strictly between the original parties, and where no one has changed his situation in reliance upon the contract and in ignorance of the secret oral condition attached to the delivery." 331 scriber may be estopped to show that his subscription was delivered conditionally, under the principle that a person who, by his words or conduct, willfully causes another to believe in the existence of a certain state of facts, and thereby induces him to act on that belief so as to alter his previous condition, is estopped to deny the existence of those facts to the other's prejudice. This principle was applied in a Minnesota case in which the defendant had delivered a subscription to the stock of a proposed corporation to its promoter, subject to an oral condition, and other persons, without any notice of the condition, had also subscribed for stock, and paid in a large part of their subscriptions, and the corporation had been organized and engaged in business, expending large sums of money, and contracting large liabilities, all upon the strength of the subscriptions, and in ignorance of the condition attached to that of the defendant. Under these circumstances, it was held that the defendant was estopped to set up the condition for the purpose of defeating an action on his subscription.332

In a Kentucky case it was held, contrary to the doctrine above stated, that if a written subscription for stock is delivered to the corporation or its agent, -- in this case to the commissioners appointed to receive subscriptions,—with the understanding, not

380 Pym v. Campbell, 6 El. & Bl. Taylor, 30 App. Div. (N. Y.) 334. 370; Cass v. Pittsburg, Virginia & See, also, Turner's Case, 7 Ont. C. Ry. Co., 80 Pa. St. 31; Gilman (Can.) 448. Compare, however, v. Gross, 97 Wis. 224; Westman v. Krumweide, 30 Minn. 313; Davis v. Kneale, 97 Mich. 72; Benton v. Martin, 52 N. Y. 570; Sweet v. Stevens, 7 R. I. 375; Ottawa, Oswego & F. R. V. R. Co. v. Hall, 1 Bradw. (III.) 612; Great Western Telegraph Co. v. Loewenthal, 154 chine Co. v. Davis, 40 Minn. 110 III. 261; Yonkers Gazette Co. v. 12 Am. St. Rep. 701.

expressed in the writing, that it is not to take effect until the performance of a condition or happening of a contingency, the oral condition is void, and the delivery absolute. The court applied the principle governing the delivery of deeds in escrow, that a deed cannot be delivered in escrow to the grantee or obligee or his agent, and that, if it is so delivered, the condition is void, and the delivery absolute and unconditional.<sup>333</sup>

#### III. SUBSCRIPTIONS UPON SPECIAL TERMS.

§ 465. In general.—A subscription upon special terms is an absolute and unconditional subscription, which makes the subscriber a stockholder, and renders him liable as such, and for the amount of the subscription, as soon as it is accepted, but contains special terms or stipulations. Such a subscription is valid, provided the special terms or stipulations are not such as to constitute a fraud upon the other subscribers or stockholders, or upon the creditors of the corporation, and provided they are not beyond the powers conferred upon the corporation by its charter, nor contrary to law.

# § 466. Subscriptions upon special terms defined, and their effect.

As was shown in a former section, subscriptions upon special terms—sometimes called subscriptions upon conditions subsequent, and sometimes incorrectly called conditional subscriptions—are very different from subscriptions upon conditions precedent, or conditional subscriptions in the proper sense. A subscription upon condition precedent, or conditional subscription, is a subscription which, while it is a binding contract, does not make the subscriber a stockholder, or render him liable to pay the amount thereof, until the performance or fulfillment of some condition.<sup>334</sup> A subscription upon special terms,<sup>335</sup> on the other hand, is an absolute and unconditional subscription. It makes the subscriber a stockholder, and renders him absolutely liable to pay the amount thereof according to its terms,

<sup>333</sup> Wight v. Shelby R. Co., 16 B. 335 1 Morawetz, Priv. Corp. § 78 Mon. (Ky.) 4, 63 Am. Dec. 522. et seq. 334 Ante, §§ 456, 461.

from the time it is accepted, but contains special terms limiting the liability of the subscriber, or imposing particular obligations upon the corporation. In the latter case, performance of the stipulations by the corporation is not a condition precedent to liability on the part of the subscriber, but is an independent or collateral agreement, for a breach of which the corporation will be liable in damages.336 Thus, an absolute and unconditional subscription to stock in a railroad company may stipulate, not as a condition precedent, but as a special term or collateral contract, that the company shall construct its road along a certain route, or that it shall establish a depot at a certain point. Performance of the stipulation is not necessary to render the subscriber liable on his subscription, and entitle the corporation to make and collect calls. Nor is it a condition precedent to the subscriber's becoming a stockholder. It is an absolute subscription for these purposes. Failure of the corporation to perform the stipulation merely gives the subscriber a right of action against it.337

336 McMillan v. Maysville & Lex- 378; North Missouri R. Co. v. agton R. Co., 15 B. Mon. (Ky.) Winkler, 29 Mo. 318; American ington R. Co., 15 B. Mon. (Ky.) 218, 61 Am. Dec. 181; Henderson & Nashville R. Co. v. Leavell, 16 B. Mon. (Ky.) 358; Paducah & Memphis R. Co. v. Parks, 86 Tenn. 554; Morrow v. Nashville Iron & Steel Co., 87 Tenn. 262, 10 Am. St. Rep. 658, 2 Keener's Cas. 989; Red land & Gulf R. Co., 81 Ga. 725; Chamberlain v. Painesville & Hudson R. Co., 15 Ohio St. 225; Miller form certain specified acts. igan Air Line R. Co., 24 Mich. 389; Belfast & Moosehead Lake Ry. Co. itants of Brooks, 60 Me. 568; Bucksitants of Brewer, 67 Me. 295; Mc- er's Cas. 989. Ginnis v. Kortkamp, 24 Mo. App.

Building & Loan Ass'n v. Rainbolt,

48 Neb. 434.

"A subscription on a condition subsequent," says Mr. Cook, "contains a contract between the corporation and the subscriber, whereby the corporation agrees to do Wing Hotel Co. v. Friedrich, 26 some act, thereby combining two Minn. 112; Johnson v. Georgia Mid-contracts, one the contract of subscription, the other an ordinary contract of the corporation to perv. Pittsburgh & Connellsville R. subscription is valid and enforce-Co., 40 Pa. St. 237, 80 Am. Dec. able, whether the conditions are 570; Connecticut & Passumpsic performed or not. The condition River R. Co. v. Bailey, 24 Vt. 465, subsequent is the same as a sepa-58 Am. Dec. 181; Lane v. Brainerd, rate collateral contract between 30 Conn. 565; Swartwout v. Mich- the corporation and the subscriber, for breach of which an action for damages is the remedy." Cook, v. Moore, 60 Me. 561; Belfast & Stock & Stockholders, § 78, quoted Moosehead Lake R. Co. v. Inhab- with approval in Morrow v. Nashville Iron & Steel Co., 87 Tenn. port & Bangor R. Co. v. Inhab- 262, 10 Am. St. Rep. 658, 2 Keen-337 Paducah & Memphis R. Co.

Stipulations, not amounting to conditions precedent, as to the time or medium of payment, makes the subscriber a stockholder as soon as it is accepted, although, of course, if the stipulations are valid, they fix the extent of the subscriber's liability.338

Special terms in a subscription may, as in the case of any other contract, be abrogated by a subsequent agreement between the subscriber and the corporation, and after the new agreement they cannot longer be enforced. Thus a special agreement between a subscriber and the corporation that the stock shall be paid for by crediting dividends is abrogated or rescinded by a new agreement under which the subscriber gives a stock note for the amount of his subscription, and he cannot set up the original agreement to defeat an action on the note. 339

# § 467. Power to accept subscriptions upon special terms, and validity thereof.

(a) In general.—In the absence of restrictions in its charter, a corporation, under its general power to contract, has the power to accept subscriptions upon any special terms not prohibited by positive law, or contrary to public policy, provided they are not such as to require the performance of acts which are beyond the powers conferred upon the corporation by its charter, and provided they do not constitute a fraud upon other subscribers or stockholders, or upon persons who are or may become creditors of the corporation.340

Subject to the limitations above stated, a subscription for stock may contain special terms as to the time, mode, or medium of payment.341 Where a corporation is authorized by its char-

v. Parks, 86 Tenn. 554; Henderson Navigation Co., 2 Ired. Eq. (N. C.) & Nashville R. Co. v. Leavell, 16 444. B. Mon. (Ky.) 358; and other cases cited in the note preceding.

338 Under a subscription for a certain amount of stock, which provides that a certain percentage only shall be payable in any one year, the subscriber becomes a stockholder at once, in the absence of a provision to the contrary. Attorney General v. Cape Fear (N. C.) 444.

339 McDowell v. Chicago Steel Works, 124 Ill. 491, 7 Am. St. Rep.

340 Paducah & Memphis R. Co. v. Parks, 86 Tenn. 554; Roberts v. Mobile & Ohio R. Co., 32 Miss. 373.

341 Attorney General v. Cape Fear Navigation Co., 2 Ired. Eq. ter to collect installments on subscriptions at such times as may be required by the president and directors, it may accept subscriptions containing special terms as to the calls for installments.342

As was shown in a former chapter, there is nothing, in the absence of constitutional or statutory restrictions, to prevent a corporation from accepting subscriptions for stock under a special agreement by which they are to be paid in property, labor, or services, provided the agreement is free from fraud, and the property, labor, or services are of such value as to be a fair equivalent for the stock, and provided it is within the general powers of the corporation to contract therefor. 343

A subscription for stock in a railroad company may stipulate that the road shall be constructed along a certain route, 344 that the money paid upon the subscription shall be expended upon a certain part of the road,345 that a depot shall be established and maintained at a certain point, 346 that it shall be operated under certain conditions,347 that it shall expend a certain sum within a specified time in the construction of its road.348

Where a corporation sells stock, it may do so on special terms not prohibited by its charter or by statute, and not in fraud of creditors. An agreement by which a purchaser of stock may, at his option, at the end of a certain time, return the stock and receive back the price, is in the nature of a conditional sale, with an option to the purchaser to rescind, and if the rights of creditors are not involved, it is valid. It is not objectionable as a contract by the corporation to purchase its own stock.<sup>349</sup>

 $^{342}\,\mathrm{Roberts}$  v. Mobile & Ohio R. Co., 32 Miss. 373.

343 Ridgefield & New York R. Co. v. Brush, 43 Conn. 86. And see ante, §§ 384, 390(b). Compare, however, Henry v. Vermillion & Ashland R. Co., 17 Ohio, 187.

344 McMillan v. Maysville & Lexington R. Co., 15 B. Mon. (Ky.) 218, 61 Am. Dec. 181; Swartwout v. Michigan Air Line R. Co., 24 Mich. 389; Belfast & Moosehead Lake R. Co. v. Inhabitants of Brooks, 60 Me. 568.  345 Lane v. Brainerd, 30 Conn.
 565; Hanover Junction & Susquehanna R. Co. v. Grubb, 82 Pa. St. 36; Milwaukee & Northern Illinois-R. Co. v. Field, 12 Wis. 340.

848 Paducah & Memphis R. Co. v. Parks, 86 Tenn. 554.

347 Johnson v. Georgia Midland & Gulf R. Co., 81 Ga. 725.

348 Connecticut & Passumpsic Rivers R. Co. v. Bailey, 24 Vt. 465, 58 Am. Dec. 181.

349 Bent v. Duluth Coffee & Spice-Co., 64 Minn. 307; Browne v. St.

### (b) Violation of charter, statutory, or constitutional provisions.

-A corporation clearly has no power to agree with subscribers upon special terms which are in violation of express charter, statutory, or constitutional provisions. If it does so, the special terms, as a general rule, are void, not only as against subsequent creditors, but also as against the corporation itself, and they cannot be set up either to defeat an action upon the subscriptions, or as the foundation of an action against the corporation. 850 This principle has frequently been applied to special agreements, by which subscriptions are to be paid in part only, or by which the money paid thereon is to be returned directly or indirectly to the subscribers, where the charter of the corporation or general statutory or constitutional provisions require payment in full,351

An agreement that payment of a subscription shall be delayed beyond the time within which the charter requires it to be paid is void for want of power on the part of the corporation to make it.352

A stipulation that a subscription may be paid in property,

ley, 92 Ill. App. 287, and note 355,

A provision in a contract of sale of stock by a corporation that the purchaser can return it "after six months," if dissatisfied, requires that the option to return it shall be exercised, if at all, within a reasonable time after expiration of the six months. New Haven Trust Co. v. Gaffney, 73 Conn. 480.

350 Morrow v. Nashville Iron &

Steel Co., 87 Tenn. 262, 10 Am. St. Rep. 658, 2 Keener's Cas. 989; Evansville, I. & C. Straight Line R. Co. v. City of Evansville, 15 Ind. 395; Thigpen v. Mississippi Central R. Co., 32 Miss. 347; Clarke v. Omaha & Southwestern R., 4 Neb. 458; Noble v. Callender, 20 Ohio St. 199.

351 Morrow v. Nashville Iron & Steel Co., 87 Tenn. 262, 10 Am. St.

Paul Plow Works, 62 Minn. 90. Rep. 658, 2 Keener's Cas. 989. In Compare Vance & Jones Co. v. Bent- this case, where subscriptions were required by statute to be paid in full at their par value, it was held that a stipulation in a contract with a subscriber that he should receive, in addition to his shares of stock, interest-bearing bonds to an equal amount, secured by a mortgage on the company's plant, was absolutely void, both as against creditors, and as be-tween the subscriber and the corporation, and that failure of the corporation to carry out the stipulation did not release him from liability on his subscription. See also, Mann v. Cooke, 20 Conn. 178; Thigpen v. Mississippi Central R. Co., 32 Miss. 347; Knox v. Childersburg Land Co., 86 Ala. 180. Other cases are referred to in a former chapter. See ante, § 389 et seq.

352 Thigpen v. Mississippi Cen-

tral R. Co., 32 Miss. 347.

labor, or services is void if the charter requires payment in money.353

(c) Special terms constituting a fraud upon other subscribers or creditors.—A corporation has no authority to accept subscriptions upon special terms, where the terms are such as to constitute a fraud upon the other subscribers, or upon persons who may become creditors of the corporation in reliance upon a bona fide and regular subscription of the authorized capital stock. In such a case, however, the subscription is not void. The fraudulent and unauthorized stipulations are void, and the subscriber is liable on his subscription as if no such stipulations had been inserted. 354 It has been held, therefore, in many cases, that any secret agreement between a subscriber for stock in a corporation and the corporation or its agents or promoters, by which he is allowed to subscribe upon different terms than other subscribers, since it is a fraud upon the latter, and any secret agreement by which he is to be released in whole or in part from liability on his subscription, since it is a fraud both upon the other subscribers and upon persons who afterwards become creditors of the corporation, is void, and the subscription may be enforced by the corporation, or by or for the benefit of creditors, as if no such agreement had been made.355

s53 Clarke v. Omaha & Southwestern Railroad, 4 Neb. 458; Noble v. Callender, 20 Ohio St. 199; Baile v. Calvert College Educational Society, 47 Md. 117.

354 Upton v. Tribilcock, 91 U. S.
45, 1 Cum. Cas. 824; Mann v.
45, 1 Cum. Cas. 824; Fleece v. Indiana & Illinois Central R. Co., 8
Blackstone, 31 Ill. 538, 83 Am. Dec. Ind. 460; New Albany & Salem R. 246; Melvin v. Lamar Ins. Co., 80 Co. v. Fields, 10 Ind. 187; Chouteau III. 446, 22 Am. Rep. 199, 2 Smith's Ins. Co. v. Floyd, 74 Mo. 286; Pis- Cas. 852, 2 Keener's Cas. 1197; Ins. Co. v. Floyd, 74 Mo. 286; Piscataqua Ferry Co. v. Jones, 39 N.
H. 491; Miller v. Hanover Junction & Susquehanna R. Co., 87 Pa.
St. 95; Downie v. White, 12 Wis.
176, 78 Am. Dec. 731; Robinson v.
Pittsburgh & Connellsville R. Co., 32 Pa. St. 334, 72 Am. Dec. 792; Southwestern R. Co., 4 Neb. 458; Webster v. Upton, 91 U. S. 65; Martin v. South Salem Land Co., 94
Va. 28; Wilson v. Hundley, 96 Va.

1453

A stipulation in a contract of subscription that it shall be payable only on the call of the directors is valid as between the stockholders, but will not prevent enforcement of the subscription to pay debts of the corporation.<sup>356</sup>

Of course, stipulations in a subscription, as a stipulation that the whole or a part of it need not be paid, or will be returned,

39 N. H. 491; Wetherbee v. Baker, 35 N. J. Eq. 501; Phoenix Warehousing Co. v. Badger, 6 Hun (N. Y.) 293, 67 N. Y. 294; Meyer v. Blair, 109 N. Y. 600, 4 Am. St. Rep. 500; Marshall Foundry Co. v. Killian, 99 N. C. 501, 6 Am. St. Rep. v. Fields, 10 Ind. 187; Nickerson v. English, 142 Mass. 267; Henry v. Vermillion & Ashland R. Co., 17 Ohio, 187; Bates v. Lewis, 3 Ohio St. 459; Robinson v. Pittsburgh & Connellsville R. Co., 32 Pa. St. 334, 72 Am. Dec. 792; Miller v. Han-over Junction & Susquehanna R. Co., 87 Pa. St. 95; La Grange & Monticello Plank Road Co. v. Mays, 29 Mo. 64; Chouteau Ins. Co. v. Floyd, 74 Mo. 286; Haskell v. Sells, 14 Mo. App. 91; Blodgett v. Morrill, 20 Vt. 509; Connecticut & Passumpsic Rivers R. Co. v. Bailey, 24 Vt. 465, 58 Am. Dec. 181; Downie v. White, 12 Wis. 176, 78 Am. Dec. 731; Webster v. Upton, 91 U. S. 65; Jewell v. Rock River Paper Co., 101 Ill. 57; Wilson v. Hundley, 96 Va. 96,

A secret agreement entered into between the directors of a railroad company and a subscriber for shares therein, that he may, within a certain time, reduce the number of shares subscribed for, the subscription being held out as bona fide for the full amount in order to induce others to subscribe, is void as a fraud upon the other subscribers, and the subscription may be enforced for the full amount by the corporation. White Mountains R. Co. v. Eastman, 34 N. H. 124.

An agreement that repayment of part of the amount of subscriptions to the capital stock of a corporation shall be secured by a

124; Piscataqua Ferry Co. v. Jones, mortgage to be given by the corposor N. H. 491; Wetherbee v. Baker, ration to the subscribers is void, 35 N. J. Eq. 501; Phoenix Wareas a fraud upon creditors. Boney housing Co. v. Badger. 6 Hun (N. v. Williams, 55 N. J. Eq. 691.

A secret agreement between a corporation and a subscriber for stock, that the corporation will buy the stock back at any time after two years at a premium, besides paying a dividend in the meantime, is illegal and void as against creditors. Vance & Jones Co. v. Bentley, 92 Ill. App. 287. Compare the cases in note 349, supra.

A guaranty given by a corporation to subscribers to its stock, that they shall not be called on to pay more than a certain per cent. on the par value, cannot be enforced by the subscribers as against creditors of the corporation who had no notice of the agreement when their debts were contracted. Martin v. South Salem Land Co., 94 Va. 28

A note given for a subscription to stock in an insurance company, for the purpose of increasing the subscriptions to the amount required by statute as a condition precedent to organization, is payable absolutely, notwithstanding a private agreement that, after passing the examination of the commissioners provided for by law for the purpose of ascertaining the fact of subscription of the required amount of capital, it shall be surrendered, and a note for a less amount substituted. The private agreement is a fraud upon the law. and the maker of the note remains liable, although the note has been surrendered and destroyed. Tuckerman v. Brown, 33 N. Y. 297, 88 Am. Dec. 386.

356 Curry v. Woodward, 53 Ala. 371.

cannot constitute a fraud upon the other stockholders if they Such a stipulation, therefore, is valid as between the subscriber and the corporation, in the absence of charter or statutory restrictions, if all the stockholders know of it, and expressly or impliedly consent.357 It has been held, therefore, that where a person subscribes to the capital stock of a corporation solely for the purpose of enabling it to obtain a certificate of organization, under an agreement, consented to by all the other subscribers, that he is not to be liable on the stock, or be required to pay assessments thereon, he is not liable to an assessment on the stock as against the other subscribers until an assessment becomes necessary in order to pay the debts of the corporation. "In most of the cases," said the court in such a case, "where subscriptions to the capital stock of corporations have been condemned, as being conditional, or accompanied by secret or qualifying agreements, the rights of creditors or stockholders have been prejudiced. Creditors are entitled to look to the stock as it appears upon the face of the subscription list. Each stockholder has a vested right in the contract for subscription of every other stockholder. In the case at bar, no creditor is injured, and no creditor is complaining. The appellant stockholders cannot object to the release of stock which they permitted to be subscribed for with the understanding that so far as they themselves were concerned, it should be released." 358

Nor does such an agreement constitute a fraud upon existing creditors of the corporation, where there is no withdrawal of assets, or upon persons who subsequently become creditors with notice, and they cannot complain.<sup>359</sup> It is void, however, notwithstanding the consent of all the stockholders, as against persons who subsequently become creditors of the corporation without notice, and in reliance, which will be presumed in the ab-

<sup>357</sup> Scovill v. Thayer, 105 U. S. Paving Co., 129 Ill. 64, 2 Smith's 143, 2 Keener's Cas. 897, 2 Smith's Cas. 857, 2 Keener's Cas. 1212. Cas. 818; Winston v. Dorsett Pipe See, also, Jones v. Johnson, 86 Ky. & Paving Co., 129 Ill. 64, 2 Smith's 530; Traphagen v. Sagar, 63 Minn. Cas. 857, 2 Keener's Cas. 1212. 317. And see ante, § 398.

<sup>358</sup> Winston v. Dorsett Pipe & 359 Ante, § 401(j).

sence of evidence to the contrary, upon the full amount of the capital stock being paid or secured.360

The doctrine invalidating secret agreements between the officers of a corporation and a subscriber, by which the latter is to be released in whole or in part from liability on his subscription, does not apply to agreements between the promoters or particular stockholders of a corporation and a subscriber, by which the former are to buy back his stock so as to let him out. for such an agreement as this is between the parties only, and does not affect the subscriber's liability on his subscription. Such an agreement is not a fraud upon other subscribers.<sup>361</sup>

(d) Agreement to pay interest.—A corporation may stipulate to pay subscribers interest on sums paid in by them on their subscriptions before the time when they are bound to pay by the terms of their contract, or prior to the commencement of regular business, provided such an agreement is not prohibited by the charter or general law, and provided creditors and other stockholders are not prejudiced;362 but it cannot do so in viola-

143, 2 Keener's Cas. 897, 2 Smith's for by him, they would take it and Cas. 818. And see ante, § 401.

is no design to deceive or defraud 50. any one, although none of the sub-scriptions are to be paid until all Massachusetts R. Co., 44 Vt. 613; the stock is reliably subscribed, Wright v. Vermont & Massachu-and other subscribers neither have setts R. Corp., 12 Cush. (Mass.) such an agreement as to their 68; City of Ohio v. Cleveland & stock nor are aware of the agreement in question. Morgan v. Struthers, 131 U. S. 246; Meyer v. Blair, 109 N. Y. 600, 4 Am. St. Rep.

Where subscribers who had paid for their stock in order to induce subscribers who had repudiated stock subscribed for agreed with one of the latter, without the 534. knowledge of the others, that, if

360 Scovill v. Thayer, 105 U.S. he would take the stock subscribed give him a note for the price, it 361 An agreement between the was held that the agreement was promoters of a corporation and a not a fraud upon the other repusubscriber that the former will diating subscribers, and that the take the latter's shares and refund note given in pursuance thereof his money if he shall demand it was valid. Traphagen v. Sagar, within a certain time is valid as 63 Minn. 317. See, also, Rogers v. between the parties, where there Burr, 105 Ga. 432, 70 Am. St. Rep.

Toledo R. Co., 6 Ohio St. 489; Mc-Laughlin v. Detroit & Milwaukee Ry. Co., 8 Mich. 100; Hetfield v. Addicks, 154 Pa. St. 1; Porter v. Beacon Construction Co., 154 Pa. St. 8; Lock v. Queensland Investment & Land Mortgage Co. [1896] App. Cas. 461, affirming [1896] 1 their subscriptions to take the Ch. 397. Compare Painesville & Hudson R. Co. v. King, 17 Ohio St.

Interest is sometimes expressly

tion of charter or statutory provisions, or in fraud of some of the stockholders, or to the prejudice of creditors.<sup>363</sup>

Subscriptions for stock in a gas company, after providing that the subscriptions shall be payable in certain installments, may permit payments in full at any time, and stipulate for payment of interest on anticipated payments.364

A railroad company has the power to stipulate that each stockholder shall be entitled to interest on sums paid on stock subscriptions while its road is in process of construction, until it is completed and goes into operation, the interest being payable whenever the surplus earnings shall enable the company to make the payments, for such an agreement does not interfere with the rights of creditors, and is not contrary to public policy. 365

Agreements to pay interest by way of dividends are elsewhere considered. 366

(e) Oral stipulations—Other writings.—The general rule excluding parol evidence to add to or vary a written contract pre-

provided for by the charter or enabling act. See Hardin County v. Louisville & Nashville R. Co., 92 Ky. 412.

A stockholder cannot be compelled to accept a bond instead of money for interest due. McLaughlin v. Detroit & Milwaukee Ry. Co., 8 Mich. 100.

As to the mode of payment where the legislature authorized a corporation to issue additional stock to enable it to "provide for and pay interest" on installments paid in, see Attorney General v. City of New York, 3 Duer (N. Y.)

City of New York, 3 Duer (N. 1.)
119; Manice v. Hudson River R.
Co., 3 Duer (N. Y.) 426.
363 Sullivan v. Portland & Kennebec R. Co., 4 Cliff. 212, Fed. Cas.
No. 13,596, 94 U. S. 806; Troy &
Boston R. Co. v. Tibbits, 18 Barb.
(N. Y.) 297; Painesyillo & Hudson (N. Y.) 297; Painesville & Hudson R. Co. v. King, 17 Ohio St. 534; Pittsburg & Connellsville R. Co. v. County of Allegheny, 63 Pa. St. 126. And see post, §§ 519, 523(f).

364 Hetfield v. Addicks, 154 Pa. St. 1; Porter v. Beacon Construc-

tion Co., 154 Pa. St. 8.

365 Richardson v. Vermont & Massachusetts R. Co., 44 Vt. 613; Ryan v. Miami Valley R. W. Co., 6 Ohio Dec. 1071. Compare Painesville & Hudson R. Co. v. King. 17 Ohio St. 534.

Under a stipulation that all subscribers for stock in a railroad company shall "be allowed interest on all sums paid by them up to the time when the road shall be completed and put in operation," the interest is not payable until the road is completed and put in operation. Wright v. Vermont & Massachusetts R. Corp., 12 Cush. (Mass.) 68; Waterman v. Troy & Greenfield R. Co., 8 Gray (Mass.) 433.

Under particular statutes, see Hardin County v. Louisville & Nashville R. Co., 92 Ky. 412; Attorney General v. City of New York, 3 Duer (N. Y.) 119; Manice v. Hudson River R. Co., 3 Duer (N. Y.) 426; Pittsburg & Connellsville R. Co. v. County of Allegheny, 63 Pa. St. 126.

366 Ante, § 420; post, § 516 et seq.

vents a subscriber from adding to or varying a complete and unambiguous written contract of subscription by proof of prior or contemporaneous oral stipulations or agreements, unless they were omitted from the writing by fraud or mistake.367

It has been held, very properly, that when a written subscription is unambiguous and complete on its face, special terms which would operate as a fraud on other subscribers or creditors cannot be proved by a separate contemporaneous written in-This, however, cannot be true except where the strument.368 special terms are secret, so that to allow such proof would operate as a fraud upon other subscribers or creditors. A letter accompanying a contract of subscription has been held admissible to show that the subscription was upon special terms. 369

# (f) Authority of agents receiving subscriptions.—The validity

gia R. Co., 8 Fla. 370, 73 Am. Dec. 713; Johnson v. Pensacola & Georgia R. Co., 9 Fla. 299; Piscataqua Ferry Co. v Jones, 39 N. H. 491; Ala. 640; Blodgett v. Morrill, 20 Vt. 509; Kennebec & Portland R. Co. v. Waters, 34 Me. 369; Phoenix Warehousing Co. v. Badger, 6 Hun (N. Y.) 293, 67 N. Y. 294; Kelsey v. Northern Light Oil Co., 45 N. Y. 505; Ridgefield & New York R. Co. v. Brush, 43 Conn. 86; Thigpen v. Mississippi Central R. Co., 32 Miss. 347; Dill v. Wabash Valley R. Co., 21 Ill. 91; Corwith v. Culver, 69 Ill. 502; Stone v. Vandalia Coal & Coke Co., 59 Ill. App. 536; Cincinnati, Union & Ft. W. R. Co. v. Pearce, 28 Ind. 502; Low v. Studabaker, 110 Ind. 57; Noble v. Callender, 20 Ohio St. 199; Jack v. Naber, 15 Iowa, 450; Blair v. Buttolph, 72 Iowa, 31; Tabor & Northern Ry. Co. v. McCormick, 150 Iowa, 446; Migricaling Overhite. 90 Iowa, 446; Mississippi, Ouachita & R. R. R. Co. v. Cross, 20 Ark. 443; Scarlett v. Academy of Music, 46 Md. 132; Masonic Temple Ass'n

367 Martin v. Pensacola & Geor- ka Exposition Ass'n v. Townley, 46 Neb. 893; Topeka Mfg. Co. v. Hale, 39 Kan. 23; La Grange & Monti-cello Plank Road Co. v. Mays, 29 Mo. 64; Ollesheimer v. Thompson Marshall Foundry Co. v. Killian, 99 Mfg. Co., 44 Mo. App. 172; New-N. C. 501, 6 Am. St. Rep. 539; land Hotel Co. v. Wright, 73 Mo. Wight v. Shelby R. Co., 16 B. Mon. App. 240; Eakright v. Logansport & (Ky.) 5, 63 Am. Dec. 522; Wurtz-Northern Indiana R. Co., 13 Ind. burger v. Anniston Rolling Mills, 94 404; Brownlee v. Ohio, Indiana & 404; Brownlee v. Ohio, Indiana & Illinois R. Co., 18 Ind. 68; Jewell v. Rock River Paper Co., 101 Ill. 57; Libby v. Mt. Monadnock Mineral Spring & Land Co., 68 N. H. 444: Philadelphia & Delaware County R. Co. v. Conway, 177 Pa. St.

This rule does not apply to the full extent in Pennsylvania. See ante, § 460, and cases there cited.

As to parol evidence to show that a written subscription was on conditions precedent, see ante, §

Parol evidence is admissible to show false representations for the purpose of showing fraud. See post, § 468 et seq.

368 Brownlee v. Ohio, Indiana & I. R. Co., 18 Ind. 68. And see White Mountains R. Co. v. Eastman, 34 N. H. 124.

369 Elliott v. New York Endowv. Channell, 43 Minn. 353; Nebras-ment Co., 73 Hun (N. Y.) 519.

and effect of subscriptions upon special terms turns sometimes upon the extent of the authority of the officer or agent by whom they are received. If the stockholders or the directors or other managing officers of a corporation appoint an agent to solicit or receive subscriptions to the stock of the corporation, the agent has no authority to make special terms with subscribers, and if he undertakes to do so, the special terms are not binding upon the corporation unless they are subsequently ratified by the stockholders or managing officers. In the absence of a ratification, the subscription may be enforced without regard to the special terms.<sup>370</sup> The same is true of commissioners appointed by or under a statute to receive subscriptions preliminary to the organization of a corporation. In the absence of express authority, special terms agreed to by them on receiving a subscription will not bind the corporation unless ratified.371

Of course, as in the case of any other contract made by an agent of a corporation without authority, a subscription upon special terms, received by an agent without authority, may be ratified by the corporation, or by its directors or other managing officers, if the terms are such that they could have been authorized; and if the corporation, through its directors or managing officers, receives payments upon a subscription, with knowledge of special terms or conditions upon which it was made, agreed to by the agent receiving the subscription, although without authority, it thereby ratifies and is bound by the special terms or conditions.372

370 Robinson v. Pittsburgh & Connellsville R. Co., 32 Pa. St. 334, 72 nellsville R. Co., 32 Pa. St. 334, 72 duce the subscription. Joy v. Man-Am. Dec. 792; St. Nicholas Ins. Co. ion, 28 Mo. App. 55; Yonkers Gav. Howe, 7 Bosw. (N. Y.) 450; zette Co. v. Taylor, 30 App. Div. Philadelphia & Delaware County R. Co. v. Conway, 177 Pa. St. 364; Yonkers Gazette Co. v. Taylor, 30 App. Div. (N. Y.) 334. See Hardin Leach, 4 Jones L. (N. C.) 340. v. Sweeney, 14 Wash. 129. Compare Jefferson v. Hewitt, 103 Cal.

A promoter of a corporation canwith a subscriber to its stock be- 624.

fore incorporation, in order to in-(N. Y.) 334.

371 North Carolina R. Co. v.

372 Frankfort & Shelbyville Turnpike Co. v. Churchill, 6 T. B. Mon. (Ky.) 427, 17 Am. Dec. 159. And not bind it by a contract made see Jefferson v. Hewitt, 103 Cal.

### IV. FRAUD IN PROCURING SUBSCRIPTIONS.

§ 468. In general.—If a subscription to the capital stock of a corporation is induced by fraud upon the part of the managing officers of the corporation, or upon the part of an agent for whose fraud the corporation is responsible, the subscriber may maintain an action of deceit against the corporation, or against the individuals perpetrating the fraud, or against both; or, subject to limitations, he may rescind the contract and recover what he has paid. Fraud renders the subscription, not void, but voidable at the option of the subscriber, and he cannot rescind after he has ratified the contract, expressly or impliedly, with knowledge of the fraud, or if he has been guilty of laches, either in discovering the fraud, or in rescinding after its discovery. In some jurisdictions, he cannot rescind after the corporation has become insolvent, and it is necessary to enforce subscriptions for the benefit of creditors.

### § 469. Effect of fraud in general.

Except as explained in the sections following, a subscription for stock in a corporation, or sale of stock, is governed, in so far as the effect of fraud is concerned, by the same rules as govern other contracts. If a person is induced to subscribe for or purchase stock by fraud on the part of the managing officers of the corporation, or on the part of any other agent for whose fraud the corporation is responsible,<sup>373</sup> the subscription is generally voidable at his option, on discovery of the fraud, or within a reasonable time afterwards, or else entitles him to maintain an action for deceit, or both.<sup>374</sup>

374 England: Central Ry. Co. of Venezuela v. Kirch, L. R. 2 H. L. 99; Oakes v. Turquand, L. R. 2 H. 1 295; Posco Bivor Silver Minn.

373 Post, § 470.

L. 325; Reese River Silver Mining Co. v. Smith, L. R. 4 H. L. 64; Aaron's Reefs v. Twiss [1896] App. Cas. 273; In re Metropolitan Coal Consumers' Ass'n [1892] 3 Ch. 1; Ross v. Estates Investment Co., 3

Ch. App. 682.
United States: Tyler v. Savage,
143 U. S. 79; Upton v. Englehart,
Dill. 496, Fed. Cas. No. 16,800.

Alabama: Montgomery South-

ern Ry. Co. v. Matthews, 77 Ala. 357, 54 Am. Rep. 60.

Colorado: Zang v. Adams, 23 Colo. 408, 58 Am. St. Rep. 249.

Connecticut: Ashmead v. Colby, 26 Conn. 287.

Delaware: Kent County R. Co. v. Wilson, 5 Houst. 49.

Georgia: Atlanta & West Point R. Co. v. Hodnett, 36 Ga. 669; Weems v. Georgia Midland & Gulf R. Co., 84 Ga. 356, 88 Ga. 303.

Illinois: Melendy v. Keen, 89 Ill. 395.

Indiana: Wert v. Crawfords-

"Contracts of this description between an individual and a company, so far as misrepresentation or suppression of the truth is concerned, are to be treated like contracts between any two individuals. If one man makes a false statement which misleads another, the way in which that is to be treated affords the example for the way in which a contract is to be treated where a company makes a false statement which misleads an individual." <sup>375</sup>

This doctrine has repeatedly been applied in the case of false representations contained in the prospectus of a corporation, issued by it or its officers for the purpose of setting forth facts which will induce persons to subscribe for its stock.<sup>376</sup> But it

ville & Alamo Turnpike Co., 19 Ind. 242; Dorsey Machine Co. v. McCaffrey, 139 Ind. 545, 47 Am. St. Rep. 290.

Iowa: Coles v. Kennedy, 81 Iowa, 360, 25 Am. St. Rep. 503.

Kansas: Beal v. Dillon, 5 Kan. App. 27.

Maryland: Savage v. Bartlett, 78 Md. 561; Fear v. Bartlett, 81

Massachusetts: See Bradley v. Poole, 98 Mass. 169, 93 Am. Dec.

Michigan: Sherman v. American Stove Co., 85 Mich. 169.

Minnesota: See Columbia Electric Co. v. Dixon, 46 Minn. 263.

Mississippi: Walker v. Mobile & Ohio R. Co., 34 Miss. 245; Selina, Marion & M. R. Co. v. Anderson, 51 Miss. 829; Water Valley Mfg. Co. v. Seaman, 53 Miss. 655.

Missouri: Ramsey v. Thompson Mfg. Co., 116 Mo. 313; Union Nat. Bank v. Hunt, 76 Mo. 439.

New Hampshire: Anderson v. Scott (N. H.) 47 Atl. 607.

New Jersey: Vreeland v. New Jersey Stone Co., 29 N. J. Eq. 188, 190. And see Garrison v. Technic Electrical Works, 55 N. J. Eq. 708.

New York: Mead v. Bunn, 32 N. Y. 275; Kelsey v. Northern Light Oil Co., 45 N. Y. 505; Walker v. Anglo-American Mortgage & Trust Co., 72 Hun (N. Y.) 334;

Bosley v. National Machine Co., 123 N. Y. 550.

Pennsylvania: Spellier Electric Time Co. v. Leedom, 149 Pa. St. 185.

South Dakota: National Bank v. Taylor, 5 S. D. 99.

Tennessee: State v. Jefferson Turnpike Co., 3 Humph. (Tenn.) 305.

Texas: Strong v. Southwestern Bridge & Iron Co. (Tex.) 38 S. W. 546; Robinson v. Dickey, 14 Tex. Civ. App. 70; Park v. Kribs (Tex. Civ. App.) 60 S. W. 905.

Virginia: Crump v. United States Mining Co., 7 Grat. (Va.) 352, 56 Am. Dec. 116; Virginia Land Co. v. Haupt, 90 Va. 533, 44 Am. St. Rep. 939; Bosher v. Richmond & Harrisonburg Land Co., 89 Va. 455, 37 Am. St. Rep. 879; Carey v. Coffee-Stemming Machine Co. (Va.) 20 S. E. 778; Snead's Adm'r v. Ivanhoe Land & Improvement Co., 96 Va. 124.

Wisconsin: Waldo v. Chicago, St. Paul & F. R. Co., 14 Wis. 575; McClellan v. Scott, 24 Wis. 81.

<sup>375</sup> Per Lord Romilly, in Central Ry. Co. of Venezuela v. Kisch, L. R. 2 H. L. 99, 125.

376 Oakes v. Turquand, L. R. 2 H. L. 325; Reese River Silver Mining Co. v. Smith, L. R. 4 H. L. 64; In re Metropolitan Coal Consumers' Ass'n [1892] 3 Ch. 1; Savage v. Bartlett, 78 Md. 561; Fear v.

applies equally to oral representations made by the agents of the corporation in soliciting subscriptions, for the rule excluding evidence of prior or contemporaneous oral stipulations or agreements to add to or vary a written contract of subscription 377 does not apply to the proof of false and fraudulent representations by which the subscriber was induced to enter into the contract.378 False and fraudulent representations as to the financial condition of a corporation, contained in reports issued by it to its stockholders, will constitute fraud if either they or others rely thereon in afterwards subscribing for stock.379

Since the principles which determine what constitutes fraud, and the effect of fraud, with respect to subscriptions for stock in corporations, are substantially the same as in the case of other contracts, it is obvious that cases arising with reference to other contracts are applicable where the contract involved is a subscription for stock.880

## § 470. Want of authority on part of person making the representations.

A corporation is clearly not responsible for false and fraudulent representations inducing a subscription to its stock, if made by a stranger without any authority from the corporation or its officers, and if not ratified by the corporation, and such representations, therefore, cannot give the subscriber a right to rescind or to sue the corporation for damages.<sup>381</sup> Nor is a cor-

United States Mining Co., 7 Grat. (Va.) 352, 56 Am. Dec. 116; Bosher v. Richmond & Harrisonburg Land Co., 89 Va. 455, 37 Am. St. Rep. 879. And see Benedict v. Guardian Trust Co., 68 N. Y. Supp. 1082.

377 Ante, §§ 460, 467(e).
378 New York Exchange Co. v.
De Wolf, 31 N. Y. 273; and many

other cases hereafter cited. 379 New Brunswick & C. Railway & Land Co. v. Conybeare, 9 H. L. Cas. 711; Western Bank of Scot-land v. Addie, L. R. 1 H. L. Sc. 145. for false representations by a mere

Bartlett, 81 Md. 435; Crump v. writer on the subject of fraud, in which a large number of cases are collected, see 14 Am. & Eng. Enc.

Law, p. 12 et seq.

381 Duranty's Case, 26 Beav. 268; Cunningham v. Edgefield & Kentucky R. Co., 2 Head (Tenn.) 23; Smith v. Tallassee Branch of Central Plank-Road Co., 30 Ala. 650; Jewett v. Valley Ry. Co., 34 Ohio St. 601. And see Lynde v. Anglo-Italian Hemp Spinning Co. [1896] 1 Ch. 178.

380 For an extensive and com-stockholder, not acting as its paratively recent article by the agent, by which another was in-

poration responsible for false and fraudulent representations made by its president or other officers to induce a subscription, if they were not acting for the corporation, or if they had no authority to make the representations, or to solicit or receive subscriptions, unless their act has been ratified by it.382

It is very different, however, when representations are made by the officers or agents of the corporation having authority to solicit or receive subscriptions, even though without express authority to make the representations. As is elsewhere shown, it is well settled that a corporation is responsible for false and fraudulent representations made by its officers and agents within the scope of their employment, although such representations may not have been expressly authorized by the corporation or its stockholders. It is enough if they were made by the officer or agent while acting within the scope of his employment. 383 This principle applies to the full extent when subscriptions to the stock of a corporation are induced by false and fraudulent representations. If particular officers or agents are authorized to solicit or receive subscriptions to stock, and they make false and fraudulent representations to induce a person to subscribe. the corporation is responsible for the fraud, whether the representations were authorized or not.384

834 Central Ry. Co. of Venezuela
v. Kisch, L. R. 2 H. L. 99; Ranger
v. Great Western Ry. Co., 5 H. L.
Cas. 72; Western Bank of Scotland

duced to subscribe. Canal Bank v. New Jersey Stone Co., 29 N. J. v. Holland, 5 La. Ann. 363. Eq. 188; Garrison v. Technic Elecduced to subscribe. Canal Bank v. Holland, 5 La. Ann. 363.
v. Holland, 5 La. Ann. 363.

Sas Rives v. Montgomery South Plank-Road Co., 30 Ala. 92; Smith Waldo v. Chicago, St. Paul & F. R. v. Tallassee Branch of Central Plank-Road Co., 30 Ala. 650; Crump Southern Ry. Co. v. Matthews, 77 v. United States Mining Co., 7 Ala. 357, 54 Am. Rep. 60; Zang v. Grat. (Va.) 352, 56 Am. Dec. 116; Browning v. Hinkle, 48 Minn. 544, St. Rep. 691.

383 Ante, § 238(b); post, chapter Xxiv.

384 Central Ry. Co. of Venezuela pra.

In England it was at one time held that a corporation was not responsible for the false and fraud-Cas. 72; Western Bank of Scotland responsible for the false and fraudv. Addie, L. R. 1 H. L. Sc. 145; ulent representations made by their
Tyler v. Savage, 143 U. S. 79; agents in procuring subscriptions,
Crump v. United States Mining and there are some early decisions
Co., 7 Grat. (Va.) 352, 56 Am. Dec. to this effect in this country. Dodg116; New York Exchange Co. v. son's Case, 3 De Gex & S. 85;
De Wolf, 31 N. Y. 273; Vreeland Ayre's Case, 25 Beav. 513; Mix-

It is also well settled that a corporation may become responsible for the fraud of a person by ratification of the fraud, or by ratification of the transaction in the course of which the fraud was perpetrated. If a corporation accepts a subscription to its capital stock procured by a person without authority, it not only ratifies the act of such person in receiving the subscription, but also impliedly ratifies and becomes responsible for any false and fraudulent representations which he may have made to induce the subscription.<sup>385</sup>

Even if a corporation is not responsible, in the absence of a ratification, for false representations contained in a prospectus issued by its promoters prior to its formation, it becomes responsible if it subsequently approves or otherwise ratifies the prospectus.386

Commissioners appointed by the charter or enabling act to receive subscriptions have no authority to bind the corporations by representations or special stipulations, and as subscribers are chargeable with notice of their want of authority, if they rely on false representations made by the commissioners, they cannot hold the corporation responsible.387

Promoters.—A corporation is not responsible for the false and fraudulent representations of a promoter which induced one to subscribe for stock, where the promoter, in making the representations, was acting for himself, and not for the corporation, or where the corporation has not in any way become a

the doctrine stated in the text established. See the English and federal cases at the beginning of this note.

see Custar v. Titusville Gas & Wa-

ter Co., 63 Pa. St. 381.

er's Case, 4 De Gex & J. 575; Pay-son v. Withers, 5 Biss. 269, Fed. 178; Garrison v. Technic Electrical Cas. No. 10,864. But the doctrine Works, 55 N. J. Eq. 708; Anderson has long ago been repudiated, and v. Scott (N. H.) 47 Atl. 607; Talmadge v. Sanitary Security Co., 31 App. Div. (N. Y.) 498.

386 In re Metropolitan Coal Conis note. sumers' Ass'n [1892] 3 Ch. 1; As to the rule in Pennsylvania, Crump v. United States Mining Co., 7 Grat. (Va.) 352, 56 Am. Dec. 116.

387 Wight v. Shelby R. Co., 16 B. 385 Crump v. United States Min- Mon. (Ky.) 4, 63 Am. Dec. 522; ing Co., 7 Grat. (Va.) 352, 56 Am. Bavington v. Pittsburgh & Steuben-Dec. 116; Walker v. Mobile & Ohio ville R. Co., 34 Pa. St. 358; Nip-R. Co., 34 Miss. 245; Zang v. penose Mfg. Co. v. Stadon, 68 Pa. Adams, 23 Colo. 408, 58 Am. St. St. 256; Rutz v. Esler & Ropiequet Rep. 249; Lynde v. Anglo-Italian Mfg. Co., 3 Bradw. (Ill.) 83. party to the fraud.<sup>388</sup> But it is otherwise if the corporation has become a party to the fraud; and according to some of the cases, if the promoter was acting for the corporation, it is liable, on the ground that the corporation, in accepting the benefit of the subscription, assumes responsibility for the false representations by means of which it was obtained.<sup>389</sup>

Representations at public meetings.—By the weight of authority, a corporation is not responsible for representations made by officers of the corporation or others at a public meeting held for the purpose of advertising the undertaking, and inducing subscriptions for stock, unless such representations were made by authority of the corporation.<sup>390</sup>

Representations by committee.—It has been held that a corporation is not responsible for representations made without authority by a committee appointed prior to its formation for the purpose of procuring subscriptions.<sup>391</sup>

Province of jury.—Whether representations were authorized by the corporation, or subsequently ratified by it, is a question for the jury, unless the admitted circumstances are such as to render the corporation responsible as a matter of law, under the rules above stated.<sup>392</sup>

sss Lynde v. Anglo-Italian Hemp Spinning Co. [1896] 1 Ch. 178; Shick v. Citizens' Enterprise Co., 15 Ind. App. 329, 57 Am. St. Rep. 230; Franey v. Warner, 96 Wis. 222; Oldham v. Mt. Sterling Improvement Co., 20 Ky. Law Rep. 207.

Acts and statements of the promoters of a corporation tending to show that its real object was illegal, but which have not been adopted or acted upon by the corporation, do not entitle a subscriber to avoid his subscription. United States Vinegar Co. v. Schlegel, 143 N. Y. 537, affirming 67 Hun (N. Y.) 356.

389 Virginia Land Co. v. Haupt, 90 Va. 533, 44 Am. St. Rep. 939; ing Co., McDermott v. Harrison, 56 Hun Dec. 116 (N. Y.) 640, 9 N. Y. Supp. 184; Oil Co., Franey v. Warner, 96 Wis. 222. Georgia Compare Miller v. Wild Cat Gravel Ga. 303.

388 Lynde v. Anglo-Italian Hemp Road Co., 57 Ind. 241; Oldham v. pinning Co. [1896] 1 Ch. 178; Mt. Sterling Improvement Co., 20 nick v. Citizens' Enterprise Co., Ky. Law Rep. 207.

390 Smith v. Tallassee Branch of Central Plank Road Co., 30 Ala. 650; Mississippi, Ouachita & R. R. R. Co. v. Cross, 20 Ark. 443; First Nat. Bank of Cedar Rapids v. Hurford, 29 Iowa, 579; Buffalo & New York City R. Co. v. Dudley, 14 N. Y. 336; Vicksburg, Shreveport & T. R. Co. v. McKean, 12 La. Ann. 638.

Contra, Atlanta & West Point R. Co. v. Hodnett, 36 Ga. 669; Mc-Clellan v. Scott, 24 Wis. 81.

391 St. Johns Mfg. Co. v. Munger, 106 Mich. 90.

<sup>392</sup> Crump v. United States Mining Co., 7 Grat. (Va.) 352, 56 Am. Dec. 116; Kelsey v. Northern Light Oil Co., 45 N. Y. 505; Weems v. Georgia Midland & Gulf R. Co., 88 Ga. 303.

### § 471. What amounts to fraud in procuring subscriptions.

(a) In general.—In determining whether a fraud has been committed in procuring a subscription to stock, the same principles are to be applied as in the case of any other contract.<sup>393</sup> It may be laid down as a general rule, therefore, that any false representation of a material fact, made by a person for whose representations the corporation is responsible, with knowledge that it is false, or recklessly, and without any knowledge as to its truth or falsity, if relied upon by a person to whom it is made in subscribing for shares, is such fraud as entitles him to rescind his subscription, or maintain an action for damages.<sup>394</sup>

Among the representations which have been held to be material false representations of fact constituting fraud are representations that the corporation has purchased or owns certain property or rights,<sup>395</sup> that its property cost a certain sum,<sup>396</sup> that it is free from incumbrance,<sup>397</sup> that land owned by it contains valuable mines in profitable operation,<sup>398</sup> that all or a certain amount of the capital stock has been subscribed for, or that it has been subscribed for by particular persons,<sup>399</sup> that a cer-

393 Central Ry. Co. of Venezuela v. Kisch, L. R. 2 H. L. 99, 125.

set Central Ry. Co. of Venezuela v. Kisch, L. R. 2 H. L. 99; Ranger v. Great Western Ry. Co., 5 H. L. Cas. 72; Ramsey v. Thompson Mfg. Co., 116 Mo. 313; Savage v. Bartlett, 78 Md. 561; McClellan v. Scott, 24 Wis. 81; Coles v. Kennedy, 81 Iowa, 360, 25 Am. St. Rep. 503; Sherman v. American Stove Co., 85 Mich. 169; Melendy v. Keen, 89 Ill. 395; Selma, Marion & M. R. Co. v. Anderson, 51 Miss. 829; Water Valley Mfg. Co. v. Seaman, 53 Miss. 655; and other cases in the notes following.

Tollowing.

395 Ross v. Estates Investment
Co., 3 Ch. App. 682; Ramsey v.
Thompson Mfg. Co., 116 Mo. 313;
Waldo v. Chicago, St. Paul & F. R.
Co., 14 Wis. 575; Savage v. Bartlett, 78 Md. 561. And see Anderson v. Scott (N. H.) 47 Atl. 607;
Foulks Accelerating Air Motor Co.
v. Thies (Nev.) 65 Pac. 373.

396 Zang v. Adams, 23 Colo. 408, 58 Am. St. Rep. 249; Capel v. Sim's Ships Composition Co., 58 Law T. (N. S.) 807.

397 Water Valley Mfg. Co. v. Seaman, 53 Miss. 655; McClellan v. Scott, 24 Wis. 81.

398 Reese River Silver Mining Co. v. Smith, L. R. 4 H. L. 64.

399 Ross v. Estates Investment Co., 3 Ch. App. 682; Arnison v. Smith, 59 Law T. (N. S.) 627; Henderson v. Lacon, L. R. 5 Eq. 249; Spellier Electric Time Co. v. Leedom, 149 Pa. St. 185; Coles v. Kennedy, 81 Iowa, 360, 25 Am. St. Rep. 503; Alabama Foundry & Machine Works v. Dallas (Ala.) 29 So. 459; Talmadge v. Sanitary Security Co., 31 App. Div. (N. Y.) 498. Compare Haskell v. Worthington, 94 Mo. 560.

This does not apply, however, to a mere statement that a railroad company or other corporation has enough stock subscribed to con-

tain amount has been actually paid in,400 that the corporation is in a solvent and prosperous condition, the representation being known to be false, 401 that certain persons are directors or other officers of the corporation, or that they have agreed to act as such, 402 that not more than a certain amount of stock and bonds will be issued, where a greater amount has already been issued.403 Other cases will be referred to in the sections following.

(b) Nondisclosure or concealment of facts.—As a general rule, to constitute fraud for the purpose of avoiding a subscription to stock, as for the purpose of avoiding any other contract, there must be a false representation, and not a mere failure to disclose facts, without more. 404 A representation, however, which is true as far as it goes, may be rendered false by reason of a failure to disclose facts, or, in other words, may be half-truth only, and in such a case it will amount to fraud. This is true where a prospectus or other statement purports to be a full and

struct its road or carry out the enterprise successfully. This is mere remeter Metropolitan Coal Consumers' expression of opinion. Goodrich v. Ass'n, 62 Law T. (N. S.) 30, 64 Reynolds, 31 III. 490, 83 Am. Dec. Law T. (N. S.) 561; Id. [1892] 3 240; Hardy v. Merriweather, 14 Ind. 203; Bish v. Bradford, 17 Ind. 490; Brownlee v. Ohio, Indiana & I. R. Co., 18 Ind. 68; Parker v. Thomas, 19 Ind. 213, 87 Am. Dec.

385. And see post, § 471(e).
400 Ramsey v. Thompson Mfg.
Co., 116 Mo. 313; State v. Jefferson Turnpike Co., 3 Humph (Tenn.) 305.

401 Bell's Case, 22 Beav. 35; Tyler v. Savage, 143 U.S. 79; Dorsey Machine Co. v. McCaffrey, 139 Ind. 545, 47 Am. St. Rep. 290; Sherman v. American Stove Co., 85 Mich. 169; Melendy v. Keen, 89 III. 395; Waldo v. Chicago, St. Paul & F. R. Co., 14 Wis. 575; Union Nat. Bank v. Hunt, 76 Mo. 439.

But not exaggerated representations as to the value, present and prospective, of the assets and stock of the company, which from their nature are necessarily speculative. Columbia Electric Co. v. Dixon, 46 Minn. 463. See post, § 371(c).

402 Blake's Case, 34 Beav. 639; In Ch. 1.

403 Weems v. Georgia Midland & Gulf R. Co., 84 Ga. 356, 88 Ga. 303. Setting forth in a prospectus of a corporation plans which would require that the whole amount of a proposed issue of preferred stock should be subscribed and paid for is not a representation, to one subscribing to such stock, that none will be issued until it is all taken, so as to entitle him to rescind for fraud if it is not all taken when his shares are issued to him. Bartol v. Walton & Whann Co., 92 Fed. 13.

404 See Heymann v. European Central Ry. Co., L. R. 7 Eq. 154. And see works treating generally of fraud, particularly, 14 Am. & Eng. Enc. Law, p. 66 et seq.

Failure of the officers of a corporation to disclose to a subscriber or purchaser of stock omissions or neglect of the corporation to comply with statutory or charter provifair statement of facts, but conveys a false impression by reason of the suppression of material facts. 405

This principle applies also to oral representations. Where the agents of a corporation induced a person to subscribe for shares by representing that a certain other person, known as a successful business man of large experience, had subscribed for a number of shares, whereas such person's subscription was made merely for the purpose of influencing others, and under a secret agreement that he would not be required to pay for the shares. it was held that there was such fraud as entitled the subscriber to rescind.406

Failure to disclose facts which would be disclosed upon examination of the charter or articles of association, with a knowledge of which subscribers are chargeable, or to disclose a purpose to do things authorized thereby, cannot constitute fraud.407

(c) Expression of opinion or prediction.—As a general rule, a statement, to constitute a false and fraudulent representation. must be a representation of fact, and not a mere expression of

erty in payment of subscriptions. and making and recording statements of the affairs of the company, will not support an action against the company or the officers for fraud. Robertson v. Parks. 76

405 See Central Ry. Co. of Venezuela v. Kisch, L. R. 2 H. L. 99; Oakes v. Turquand, L. R. 2 H. L. 325; New Brunswick & C. Railway & Land Co. v. Muggeridge, 1 Drew & S. 363, 381; Walker v. Anglo-American Mortgage & Trust Co., 72 Hun (N. Y.) 334. "It appears to me that it is quite necessary to uphold this as a principle: that those who issue a prospectus holding out to the public the great advantages which will accrue to persons who will take shares in a proposed undertaking, and inviting them to take shares on the faith of the representations therein contained, are bound to state every-

sions in regard to receiving prop- from stating as facts that which is not so, but to omit no one fact within their knowledge, the existence of which might in any degree affect the nature, or extent, or quality of the privileges and advantages which the prospectus holds out as inducements to take shares." New Brunswick & C. Railway & Land Co. v. Muggeridge, 1 Drew & S. 363, 381,

> <sup>406</sup> Coles v. Kennedy, 81 Iowa, 360, 25 Am. St. Rep. 503. See, also, Virginia Land Co. v. Haupt, 90 Va. 533, 44 Am. St. Rep. 939; Alabama Foundry & Machine Works v. Dallas (Ala.) 29 So. 459.

> A representation that certain persons have subscribed is a fraud, where the fact that they are to pay or have paid in property at an overvaluation is concealed. Alabama Foundry & Machine Works v. Dallas, supra.

407 Oil City Land & Improvement thing with strict and scrupulous Co. v. Porter, 16 Ky. Law Rep. 397, accuracy, and not only to abstain 99 Ky. 254.

opinion or prediction. On statements of the latter character persons have no right to rely, and if they do so, they cannot treat them as a fraud, either for the purpose of avoiding their contract, or for the purpose of an action of deceit. 408 Thus, subscriptions for shares in a railroad company cannot be avoided because of false expressions of opinion or prediction as to the future location of the road, or as to the ability of the company to construct and equip the same, or as to the time within which, or the manner in which, it will be constructed, unless they also involve false and fraudulent representations as to past or existing facts.409 Representations as to value are almost invariably within this principle, for they are almost necessarily mere expressions of opinion. While a subscriber may rely upon positive statements of fact as to the financial condition of the company, its ownership of particular property, the nature of its property, its freedom from incumbrance, and other facts affecting the value of its assets and the advantages of the enterprise as an investment,410 he has no right to rely upon mere expressions of opinion as to the value, present or prospective, of its assets and stock, which from their nature are necessarily speculative.411 Representations as to the value of the property or stock of a cor-

408 Walker v. Mobile & Ohio R. and cannot be relied upon by a sub-Co., 34 Miss. 245; Selma, Marion & M. R. Co. v. Anderson, 51 Miss. 229; Bish v. Bradford, 17 Ind. 490; App. 329, 57 Am. St. Rep. 230. Clem v. Newcastle & Danville R. Co., 9 Ind. 488, 68 Am. Dec. 653; Hughes v. Antietam Mfg. Co., 34 Eakright v. Logansport & Northern Md. 316; Columbia Electric Co. v. Dixon, 46 Minn. 463; Union Nat. Bradford, 17 Ind. 490; Parker v. Bank v. Hunt, 76 Mo. 439; Montgomery Southern Ry. Co. v. Matthews, 77 Ala. 357, 54 Am. Rep. 60; Cal. 535; Armstrong v. Karshner,

False representations by promoters as to the objects and purposes of the proposed corporation do not relate to any past or existing fact, on, 46 Minn. 463.

Indiana R. Co., 13 Ind. 404; Bish v. Bradford, 17 Ind. 490; Parker v. Thomas, 19 Ind. 213, 81 Am. Dec. 385, 390; Jefferson v. Hewitt, 95 Cal. 535; Armstrong v. Karshner, Jefferson v. Hewitt, 95 Cal. 535; 47 Ohio St. 276; Jackson v. Stock-Bell v. Americus, Preston & L. R. Co., 76 Ga. 754; Weston v. Columbus Southern Ry. Co., 90 Ga. 289; Montgomery Southern Ry. Co. v. Matthews, 77 Ala. 357, 54 Am. Jackson v. Stockbridge, 29 Tex. Rep. 60; Bell v. Americus, Preston 394, 94 Am. Dec. 290; Shattuck v. Robbins, 68 N. H. 565.

False representations by Taxward Columbus Southern Ry. Co. 200 Co.

410 See supra, this section, (a).
411 Columbia Electric Co. v. Dix-

poration, involving no positive statement of fact, or as to the probable cost and profit of the enterprise, the dividends that will be paid, etc., are almost always mere expressions of opinion or prediction, which cannot be set up as constituting fraud.<sup>412</sup>

It has sometimes been said that, if an opinion is falsely expressed with intent to deceive, and does deceive, it will constitute fraud, so as to render a contract of subscription voidable. this is not true where there is a mere expression of opinion, and nothing more, at least unless there is some peculiar relation of trust and confidence between the parties, for the doctrine that a mere expression of opinion does not amount to fraud is based. not upon the ground that there is no intent to deceive, nor upon the ground that it does not in fact deceive, but upon the ground that persons have no right to rely upon representations or statements of such a nature, and it is due to their own folly if they do so, and are deceived. If, however, the matter to which the representation relates is a matter susceptible of exact knowledge. and material, and is not equally within the means of knowledge of both parties, a statement in the form of an expression of opinion thereon, which is known to be false, and is made with the intention that it shall be acted upon, and which is acted upon, is a false and fraudulent representation, constituting fraud, and not a mere expression of opinion. 413

A statement that the property of a corporation cost a certain sum is not a mere expression of opinion, like statements as to

A false statement by an officer Dynamite Proof a corporation that its stock is T. (N. S.) 104.

<sup>412</sup> Central Ry. Co. of Venezuela v. Kisch, L. R. 2 H. L. 99; Denton v. Macneil, L. R. 2 Eq. 352; Walker v. Mobile & Ohio R. Co., 34 Miss. 245; Union Nat. Bank v. Hunt, 76 Mo. 439; Robertson v. Parks, 76 Md. 118; Hughes v. Antietam Mfg. Co., 34 Md. 316; Columbia Electric Co. v. Dixon, 46 Minn. 463; Vawter v. Ohio & Mississippi R. Co., 14 Ind. 174; Armstrong v. Karshner, 47 Ohio St. 276; Swan v. Mathre, 103 Iowa, 261.

<sup>412</sup> Central Ry. Co. of Venezuela worth a certain sum per share is Kisch, L. R. 2 H. L. 99; Denton a mere expression of opinion, and Macneil, L. R. 2 Eq. 352; Walker does not constitute fraud, although Mobile & Ohio R. Co., 34 Miss. relied upon. Union Nat. Bank v. 5; Union Nat. Bank v. Hunt, 76 Hunt, 76 Mo. 439.

A false statement as to the value of a patent owned by a corporation is not fraud. Denton v. Macneil, L. R. 2 Eq. 352.

<sup>413</sup> Montgomery Southern Ry. Co. v. Matthews, 77 Ala. 357, 54 Am. Rep. 60. And see Scott v. Snyder Dynamite Projectile Co., 67 Law T. (N. S.) 104.

value, but is a representation of fact, which, if known to be false, will constitute a false and fraudulent representation.414

(d) Promises and statements of intention.—A representation, to constitute fraud, must relate to a past or existing fact, and not be a mere collateral promise or a statement of inten-. tion, or other statement as to future events. These are no ground for rescinding a subscription, although they may be made with intent to deceive, and may not be performed or realized.415 Thus, a subscriber for stock in a railroad company cannot avoid his subscription because of false representations or statements as to how, when, or where the road will be built, although made, not as mere expressions of opinion, but as statements of fact, 416 All promises are excluded from consideration unless incorporated as a term of the contract of subscription.

A statement of intention or other statement as to future events is not within this principle, where by implication it necessarily involves a representation as to past or existing facts, and this implied representation is false, and known to be so. One who represents that a certain thing will or will not be done or happen in the future impliedly represents that there is nothing known to him at the time of the representation by reason

58 Am. St. Rep. 249. See supra, this section, (a).

415 Bish v. Bradford, 17 Ind. 490; Parker v. Thomas, 19 Ind. 213, 81 Am. Dec. 385; Fox v. Allensville, C. S. & V. Turnpike Co., 46 Ind. 31; Armstrong v. Karshner, 47 Ohio St. 276; York Park Building Ass'n v. Barnes, 39 Neb. 834; Richelieu Hotel Co. v. International Military Encampment Co., 140 Ill. 248, 33 Am. St. Rep. 234; Walker v. Mobile & Ohio R. Co., 34 Miss. 245; Mobile & Ohio R. Co., 34 Miss. 245; Ind. 31; Armstrong v. Karshner, Saffold v. Barnes, 39 Miss. 399; 47 Ohio St. 276; Jefferson v. Hew-Jefferson v. Hewitt, 95 Cal. 535; itt, 95 Cal. 535; Wight v. Shelby R. Hughes v. Antietam Mfg. Co., 34 Co., 16 B. Mon. (Ky.) 4, 63 Am. Md. 316; Robertson v. Parks, 76 Dec. 522; Walker v. Mobile & Ohio Md. 118; Bell v. Americus, Preston R. Co., 34 Miss. 245; Chattanooga, & L. R. Co., 76 Ga. 754; Weston v. Rome & C. R. Co. v. Warthen, 98 Columbus Southern Ry. Co., 90 Ga. Ga. 599; and other cases in the 289: Swan v. Mathre, 103 Iowa, note preceding.

414 Zang v. Adams, 23 Colo. 408, 261; Columbia Electric Co. v. Dixon, 46 Minn. 463; Jackson v. Stockbridge, 29 Tex. 394, 94 Am. Dec. 290; Guarantee & Collection Co. of America v. Weil, 141 Pa. St. 511; Shattuck v. Robbins, 68 N. H. 565; Chattanooga, Rome & C. R. Co. v. Warthen, 98 Ga. 599; Chicago Building & Mfg. Co. v. Summerour, 101 Ca. 220 101 Ga. 820.

> 416 Bish v. Bradford, 17 Ind. 490; Parker v. Thomas, 19 Ind. 213, 81 Am. Dec. 385, 390; Fox v. Allens-ville, C. S. & V. Turnpike Co., 46 Ind. 31; Armstrong v. Karshner, 47 Ohio St. 276; Jefferson v. Hew-itt, 95 Cal. 535; Wight v. Shelby R.

of which it cannot be true. A representation that not more than a certain amount of stock and bonds will be issued for each mile of a railroad is a false and fraudulent representation, where a much greater amount has in fact been issued at the time of the representation.417

(e) Representations as to the law.—False representations as to the law, although relied upon by a subscriber, are no ground for avoiding his subscription, for all persons are bound to take notice of the law, and have no right to complain if they rely upon such representations.418 For example, a person who has subscribed for stock and received a certificate of stock which on its face renders him liable as a matter of law, for the par value of the stock, cannot avoid liability on the subscription because of false representations by the officers or agents of the corporation that the stock is nonassessable, or that it is only assessable for a certain per cent. of the par value, for such representations relate to the legal effect of the subscription and certificate.419 The same is true of a false representation by a railroad subscription agent to a subscriber for stock, to the effect that he will not be called upon to pay anything until the road is worked or laid out in his county, for this is as to the legal effect of his subscription.420

All persons subscribing for stock in a corporation are presumed to know the provisions of its charter and their effect, and if they are induced to subscribe by false representations of the agents of the corporation as to the powers of the corporation, or by false representations that it will do what its charter does not authorize it to do, they cannot rely upon such representa-

Gulf R. Co., 84 Ga. 356.

<sup>418</sup> Parker v. Thomas, 19 Ind. 213, 81 Am. Dec. 385; Clem v. Newcastle & Danville R. Co., 9 Ind. 488, 68 Am. Dec. 653; Upton v. Tribil-cock, 91 U. S. 45, 1 Cum. Cas. 824; Marion & M. R. Co. v. Anderson,

<sup>417</sup> Weems v. Georgia Midland & v. Crawfordsville, F. K. & Ft. W. R. Co., 11 Ind. 280.

<sup>419</sup> Upton v. Tribilcock, 91 U. S. 45, 1 Cum. Cas. 824; Webster v. Upton, 91 U.S. 65.

<sup>420</sup> Clem v. Newcastle & Danville Wight v. Shelby R. Co., 16 B. Mon. R. Co., 9 Ind. 488, 68 Am. Dec. 653. (Ky.) 4, 63 Am. Dec. 522; Selma, And see New Albany & Salem R. Co. v. Fields, 10 Ind. 187. See, 51 Miss. 829; Ellison v. Mobile & also, North Eastern R. Co. v. Rod-Ohio R. Co., 36 Miss. 572; Johnson rigues, 10 Rich. L. (S. C.) 278.

tions as ground for rescinding their subscriptions. 421 This is true, for instance, of a false representation that a railroad company has a right or intends to construct its road along a certain route, or between certain points, and similar representations, where its route or termini are fixed by its charter; 422 and of a representation that a railroad company will be aided by another company.423

Misrepresentations as to foreign laws, including the laws of another state, are misrepresentations of fact.424

- (f) Falsity of statement.—A representation, to amount to fraud, must be false. If it was in fact true, it is altogether immaterial that it was believed to be false, and made with intent to deceive. 425 When, however, a subscriber has been deceived by a prospectus, it is not necessary, in order to make out a case of fraud, to show any particular false statement. It is enough if the prospectus, taken as a whole, conveyed a false impression as to material facts, if it was intended to have this effect. 426
- (g) Knowledge that representation is false, and intent to deceive.—In England it is held that a false statement of a material fact, made by an officer or agent of a corporation with the intention that it shall be relied upon by a subscriber for stock, and which is relied upon, will constitute a fraud in law, for the purpose of rescission, although not for the purpose of an action of deceit, although made without knowledge of its falsity, nor

Mon. (Ky.) 4, 63 Am. Dec. 522; Upton v. Tribilcock, 91 U. S. 45, 1 Cum. Cas. 824; Peters v. Lincoln & Northwestern R. Co., 14 Fed. 319; Russell v. Alabama Midland Ry. Co., 94 Ga. 510; and other cases in the notes following.

Since one subscribing for stock in a railroad company was bound K. & Ft. W. R. Co., 11 Ind. 280. to take notice that it had no power to issue to its stockholders any stock in a construction company, it was held that false representations p. 63. touching the resources of the construction company, or the value of App. Cas. 273; Scott v. Snyder Dyits stock, were no ground for avoid-namite Projectile Co., 67 Law T. ing a subscription to the stock of (N. S.) 104.

421 Wight v. Shelby R. Co., 16 B. the railroad company. Russell v. Alabama Midland Ry. Co., 94 Ga.

422 Parker v. Thomas, 19 Ind. 213, 81 Am. Dec. 385; Wight v. Shelby R. Co., 16 B. Mon. (Ky.) 4, 63 Am. Dec. 522; Ellison v. Mobile & Ohio R. Co., 36 Miss. 572.

423 Johnson v. Crawfordsville, F.

<sup>424</sup> Upton v. Englehart, 3 Dill. 496, Fed. Cas. No. 16,800.

425 See 14 Am. & Eng. Enc. Law,

426 Aaron's Reefs v. Twiss [1896]

recklessly.427 In this country, however, the rule is different. The representation must have been fraudulent in fact, and therefore it must have been made with knowledge of its falsity, or recklessly and without any knowledge as to whether it was true or false. A representation, although false, and although relied upon by the subscriber, does not constitute fraud, and is neither ground for an action of deceit, nor ground for rescission, if it was made in good faith, and in the honest belief that it was true, and not recklessly.428

It has been said that the false representations, to amount to fraud, must have been made with intent to deceive. 429 properly speaking, this is not necessarily true. An intent to deceive will be conclusively presumed if the representations were known to be false, or if they were made recklessly and without any knowledge as to their truth or falsity, for a person is presumed, even in the criminal law, to have intended the natural and probable consequences of his voluntary acts. 430

(h) The representation as an inducement.—In order that a subscription may be avoided, or an action of deceit maintained, because of false and fraudulent representations, they must have been believed and relied upon by the subscriber, and a complaint or plea by the subscriber must so allege. However false and fraudulent a representation may have been, it has no effect un-

ton v. Fitzmaurice, 29 Ch. Div. 459. And see Foulks Accelerating Air Motor Co. v. Thies (Nev.) 65 Pac.

Contra, Kennedy v. Panama. New Zealand & A. Royal Mail Co., L. R. 2 Q. B. 580.

A representation in good faith that the title to corporate property is good, although false, does not amount to fraud. New Brunswick & C. Railway & Land Co. v. Conybeare, 9 H. L. Cas. 711.

428 Salem Mill-Dam Corp. v.

Ropes, 9 Pick. (Mass.) 187, 19 Am. Dec. 363; Selma, Marion & M. R. Co. v. Anderson, 51 Miss. 829; Cun- 102-104.

427 Reese River Silver Mining Co. ningham v. Edgefield & Kentucky v. Smith, L. R. 4 H. L. 64; Edging- R. Co., 2 Head (Tenn.) 23; Montgomery Southern Ry. Co. v. Matthews, 77 Ala. 357, 54 Am. Rep. 60; Keller v. Johnson, 11 Ind. 337, 71 Am. Dec. 355; Tabor & Northern Ry. Co. v. McCormick, 90 Iowa, 446; Braddock v. Philadelphia, Marlton & M. R. Co., 45 N. J. Law, 363; Nelson v. Luling, 4 Jones & S. (N. Y.) 544.

And see Goodrich v. Reynolds, 31 Ill. 490, 83 Am. Dec. 240.

429 Salem Mill-Dam Ropes, 9 Pick. (Mass.) 187, 19 Am. Dec. 363; Nelson v. Luling, 4 Jones & S. (N. Y.) 544. 480 14 Am. & Eng. Enc. Law, pp.

less it constituted a material inducement for the subscription. 431 If the subscriber knew that the representation was false, or knew facts which must have shown it to be false, he clearly cannot complain.432

Where a person subscribes for stock, and afterwards gives his note in payment, he cannot avoid liability on the ground of false and fraudulent representations made, not at the time of the subscription, but at the time the note was given.433

It is not necessary, however, that the representation shall have been the sole inducement. It is enough if it was a material inducement,—if it so contributed as an inducement that without it the subscription would not have been made,-although other inducements may also have contributed.434

(i) Right to rely upon representations.—As a general rule, if a positive representation as to a material fact is made to a person to induce him to subscribe for stock in a corporation, with the intention that he shall rely upon it, and the fact is one as to which the person making the representation can be supposed to have knowledge, the subscriber has a right to rely upon the same.

96; Parker v. Thomas, 19 Ind. 213, 81 Am. Dec. 385, 390; Smith v. Tallassee Branch of Central Plank-Road Co., 30 Ala. 650; Weems v. Georgia Midland & Gulf R. Co., 88 Ga. 303; McEacheran v. Western Transportation & Coal Co., 97 Mich. 479; Vicksburg, Shreveport & T. R. Co. v. McKean, 12 La. Ann. 638; Goff v. Hawkeye Pump & Windmill Co., 62 Iowa, 691.

A colorable subscription by a person of influence shown to another to induce him to subscribe subscription, unless he relied upon it, and was thereby induced to subscribe. Walker v. Mobile & Ohio R. Co., 34 Miss. 245.

The liability of a subscriber is not affected by false representations made by the officers of the corporation after the subscription. Bartol v. Walton & Whann Co., 92 Fed. 13.

432 Goff v. Hawkeye Pump & Ch. Div. 459.

431 Pulsford v. Richards, 17 Beav. Windmill Co., 62 Iowa, 691; Mc.; Parker v. Thomas, 19 Ind. 213, Eacheran v. Western Transportation & Coal Co., 97 Mich. 479; Benton v. Ward, 59 Fed. 411.

A person clearly cannot rescind a subscription for stock because of false statements in a prospectus or newspaper articles, or elsewhere, if he was himself an officer of the corporation, and participated in preparing the statements. Raymond v. San Gabriel Valley Land & Water Co., 10 U. S. App. 601, 53 Fed. 883.

False representations as to the does not entitle him to avoid his purpose or character of the corporation do not constitute fraud, where the subscription itself shows their falsity. Walter A. Wood Harvester Co. v. Jefferson, 71 Minn.

433 Goodrich v. Reynolds, 31 Ill. 490, 83 Am. Dec. 240.

434 Peek v. Derry, 37 Ch. Div. 541; Derry v. Peek, 14 App. Cas. 337; Edgington v. Fitzmaurice, 29

and is not bound to make independent inquiry or investigation to ascertain for himself whether it is true or false; and if a subscription, therefore, is in fact induced by a false and fraudulent representation of fact, the subscriber's right to rescind cannot be resisted by the corporation on the mere ground that he was negligent in relying upon the representation, and that he could have ascertained the truth if he had made inquiry or investigation.435

In a leading English case it was said: "When once it is established that there has been any fraudulent misrepresentation or wilful concealment by which a person has been induced to enter into a contract, it is no answer to his claim to be relieved from it to tell him that he might have known the truth by proper inquiry. He has a right to retort upon his objector, 'You, at least, who have stated what is untrue, or have concealed the truth, for the purpose of drawing me into a contract, cannot accuse me of want of caution because I relied implicitly upon your fairness and honesty." "436 And in a New York case it was said: "Every contracting party has an absolute right to rely on the express statement of an existing fact, the truth of which is known to the opposite party, and unknown to him, as the basis of a mutual engagement; and he is under no obligation to investigate and verify statements, to the truth of which, the other party to the contract, with full means of knowledge, has deliberately pledged his faith." 437

This doctrine was applied where the prospectus of a railroad company, issued for the purpose of inducing subscriptions, contained false representations as to a contract for the construction of the road, but stated that the engineer's reports, maps, plans, etc., might be inspected at the company's offices. It was held that the right of a subscriber, who relied upon the prospectus, to rescind his subscription, could not be defeated by setting up his

<sup>485</sup> Central Ry. Co. of Venezuela 81; Zang v. Adams, 23 Colo. 408, v. Kisch, L. R. 2 H. L. 99; Upton 58 Am. St. Rep. 249. v. Englehart, 3 Dill. 496, Fed. Cas. No. 16,800; Mead v. Bunn, 32 N. v. Kisch, L. R. 2 H. L. 99, 120. Y. 275; McClellan v. Scott, 24 Wis.

<sup>437</sup> Per Porter, J., in Mead v. Bunn, 32 N. Y. 275.

failure to examine the documents referred to, and which, if examined, would have shown the falsity of the prospectus. 438

A stockholder subscribing for or purchasing stock in a corporation has a right to rely upon representations of its officers as to its financial condition, without availing himself of his right to examine the books of the corporation.439 It has also been held that a subscriber may rely upon representations as to the cost of property of the corporation, and is not bound to examine the records of the corporation, or otherwise investigate, for the purpose of ascertaining the truth for himself.440

Statements made to induce subscriptions may be of such a nature, or relate to such a fact, that the person to whom they are made will have no right to rely upon them, and if this is so, he cannot treat them as ground for avoiding his subscription. Thus, as we have seen, a subscriber has no right to rely upon mere expressions of opinion,441 or upon predictions, promises, and statements of intention, or statements as to future events, 442 or upon representations as to the law.443

Even representations as to past or existing facts may be of such a nature that a subscriber cannot rely upon them. In some of the cases it has been held that a subscriber has no right to rely upon representations of fact by the agent of a corporation, where the fact is not peculiarly within the knowledge of the corporation or the person making the representation, but is equally within the means of knowledge of the subscriber, and that he cannot

J. Ch. 545.

ment which will show the untruth lows v. Fernie, L. R. 3 Ch. 477. or inaccuracy of any of its statements, and chooses not to make use Mo. 439. of his means of knowledge, but to continue in a state of willful ignorance of the facts, he cannot afterwards be heard to complain that he has been deceived by the alleged

438 Central Ry. Co. of Venezuela misstatements." It was further v. Kisch, L. R. 2 H. L. 99; Kisch v. said: "In considering the question Central Ry. Co. of Venezuela, 34 L. of knowledge or means of knowledge, it is important to see wheth-Another English case is to the er the plaintiff was a person like-contrary. It was there said: "If ly, through inexperience, to be misa person purchases shares in a com- led by a prospectus, or to place impany upon the faith of a prospec- plicit reliance upon all that it contus, and is referred to any docu- tains." Lord Chelmsford, in Hal-

439 Union Nat. Bank v. Hunt, 76

440 Zang v. Adams, 23 Colo. 408, 58 Am. St. Rep. 249.

441 Supra, this section, (c). 442 Supra, this section, (d). 443 Supra, this section, (e).

avoid his subscription in such a case because of the falsity of the representation.444

A subscriber who can read cannot avoid his subscription because of false representations as to the contents of the subscription paper.445 But an illiterate person may rely upon representations by the agent of the corporation as to the provisions of a written subscription paper, and may avoid the subscription on the ground of fraud if the paper is falsely read to him, or its provisions falsely and fraudulently misrepresented.446

It has been held that a subscriber has no right to rely upon subscriptions appearing to have been made by other persons, and that he cannot avoid his subscription on the ground that other subscriptions, apparently bona fide and absolute, were in fact fictitious, or were made under a secret agreement that they should not be paid.447 This, however, cannot be true of a positive and material false representation as to prior subscriptions.448

A subscriber has no right to rely upon representations as to the provisions of the articles of association or charter of the corporation.449

(j) Necessity for injury.—To constitute fraud, there must be some injury. In no case can a subscriber for shares avoid his subscription because of false representations, if he has not been injured or prejudiced thereby;450 as in a case where the repre-

444 Jennings v. Broughton, 22 L. Rivers R. Co. v. Bailey, 24 Vt. 465, J. Ch. 585; Thornburgh v. Newcastle & Danville R. Co., 14 Ind. 499; Walker v. Mobile & Ohio R. Co., 34 Miss. 245; Haskell v. Worthington,

In Haskell v. Worthington, 94 Co. v. Porter, 16 Ky. Law Rep. 397, Mo. 560, it was held that a sub- 99 Ky. 254. scriber could not avoid his subscriptions because of a false representation that certain other persons had also subscribed, where he had ample opportunity to ascertain be false. Walter A. Wood Harvesthe truth of the representation. ter Co. v. Jefferson, 71 Minn. 367.

445 Thornburgh v. Newcastle & Danville R. Co., 14 Ind. 499.

mo Turnpike Co., 19 Ind. 242.

58 Am. Dec. 181.

448 Coles v. Kennedy, 81 Iowa, 360, 25 Am. St. Rep. 503, as to which, see supra, this section, (a). 449 Oil City Land & Improvement

Representations as to the character or purpose of the corporation do not constitute fraud where the subscription itself shows them to

450 Ship v. Crosskill, L. R. 10 Eq. 73; Keller v. Johnson, 11 Ind. 337, 448 Wert v. Crawfordsville & Ala-o Turnpike Co., 19 Ind. 242. The Edgefield & Kentucky R. Co., 2 447 Connecticut & Passumpsic Head (Tenn.) 23; American Buildsentation, although false when made, is afterwards made good;451 or where the alleged fraud consists in concealment of the fact that other subscriptions, apparently absolute, were in fact conditional or upon special terms, if the conditions or special terms are void, and such subscriptions are therefore en-

### § 472. Remedies of subscriber or purchaser in case of fraud.

Rescission in general.—When a person is induced to enter into a contract of subscription or to purchase stock by false and fraudulent representations, he has several remedies. On discovery of the fraud, or within a reasonable time afterwards, he may rescind or repudiate his contract, and maintain a suit in equity to cancel the same, and be relieved from further liability as a stockholder, and for other relief, if he has not waived or lost his right to rescind, as will be hereafter explained. 453 may set up the fraud as a defense in an action at law by the corporation, or in a suit in equity, to recover the amount of the subscription, or of an assessment thereon, or the price in case of a sale, or in an action upon a note given by him in payment. 454

ing & Loan Ass'n v. Bear, 48 Neb.

forceable absolutely.452

451 Ship v. Crosskill, L. R. 10 Eq.

452 Anderson v. Newcastle & Richmond R. Co., 12 Ind. 376, 74 Am. Dec. 218; Connecticut & Passumpsic Rivers R. Co. v. Bailey, 24 Vt. 465, 58 Am. Dec. 181; Wilson v. Hundley, 96 Va. 96. See, also, post, § 467. Compare Coles v. Kennedy, 81 Iowa, 360, 25 Am. St. Rep. 503, ante, § 471(b).

453 Vreeland v. New Jersey Stone Co., 29 N. J. Eq. 188; Tyler v. Savage, 143 U.S. 79; Sherman v. American Stove Co., 85 Mich. 169; Bosley v. National Machine Co., 123 N. Y. 550; Bosher v. Richmond 455, 37 Am. St. Rep. 879; Carey v. Coffee Stemming Machine Co. (Va.)

20 S. E. 778; Ashmead v. Colby, 26 v. Baynes, 36 L. J. Exch. 183; Conn. 287; Negley v. Hagerstown Crossman v. Penrose Ferry Bridge

provement Co., 86 Md. 692; Coles v. Kennedy, 87 Iowa, 360, 25 Am. St. Rep. 503; Waldo v. Chicago, St. Paul & F. R. Co., 14 Wis. 575; Barcus v. Gates, 32 C. C. A. 337, 89 Fed. 783; Garrison v. Technic Electrical Works, 55 N. J. Eq. 708; Mc-Clanahan v. Ivanhoe Land & Improvement Co., 96 Va. 124.

It has been held that a number

of persons who have been induced by the same fraud to subscribe for stock in a corporation may join in a suit to cancel their subscriptions and recover what they have paid. Bosher v. Richmond & Harrisonburg Land Co., 89 Va. 455, 37 Am. St. Rep. 879; Carey v. Coffee-Stemming Machine Co. (Va.) 20 Va. 778. & Harrisonburg Land Co., 89 Va. And see Sherman v. American Stove Co., 85 Mich. 169.

Manufacturing, Mining & Land Im- Co., 26 Pa. St. 69; Davis v. Du-

Or, subject to same limitations, he may do so in a suit by a receiver or assignee for the benefit of creditors, or in a suit by a creditor or creditors.455

(b) Recovery of money or other consideration paid.—When a subscriber rescinds his subscription for fraud, and returns or tenders back his shares, he may maintain an action against the corporation to recover back what he has paid on the subscription, whether in money or property, 456 or he may recover the same in a suit in equity to cancel the subscription. 457

Officers or agents of a corporation who have received payments on a subscription induced by their false and fraudulent representations are liable therefor to the subscriber, on his rescission of the contract, in an action for money had and received.458

(c) Action for deceit.—Instead of repudiating the contract, he may, if he chooses, ratify the same, and maintain an action to recover damages for the deceit, either against the corporation,459 or against the directors or other officers or agents or promoters

mont, 37 Iowa, 47; Weems v. Geor- v. Kennedy, 81 Iowa, 360, 25 Am. gia Midland & Gulf R. Co., 84 Ga. 556; Spellier Electric Time Co. v. Leedom, 149 Pa. St. 185; Melendy v. Keen, 89 Ill. 395; Virginia Land Co. v. Haupt, 90 Va. 533, 44 Am. St. Rep. 939; Water Valley Mfg. Co. v. Seaman, 53 Miss. 655; Anderson v. Scott (N. H.) 47 Atl. 607; Zang v. Adams, 23 Colo. 408, 58 Am. St. Rep. 249; Beal v. Dillon, 5 Kan. App. 27.

455 Savage v. Bartlett, 78 Md. 561; Fear v. Bartlett, 81 Md. 435; Zang v. Adams, 23 Colo. 408, 58 Am. St. Rep. 249. See post, § 473

456 Grangers' Ins. Co. v. Turner, 61 Ga. 561; Hamilton v. Grangers' Life & Health Ins. Co., 67 Ga. 145; Ramsey v. Thompson Mfg. Co., 116 Mo. 313; Sherman v. American Stove Co., 85 Mich. 169; Booth v. Smith, 18 Ill. App. 266.

erford, 74 Ga. 435; Boscher v. Rich-Va. 455, 37 Am. St. Rep. 879; Coles fraud.

St. Rep. 503; Barcus v. Gates, 32 C. C. A. 337, 89 Fed. 783; McClanahan v. Ivanhoe Land & Improvement Co., 96 Va. 124.

458 Jarrett v. Kennedy, 6 C. B.

319; post, chapter xxiv.

459 Dorsey Machine Co. v. McCaffrey, 139 Ind. 545, 47 Am. St. Rep. 290; Peebles v. Patapsco Guano Co., 77 N. C. 233. And see

ante, § 238(b).

In Wilson v. Hundley, 96 Va. 96, it was held that, when a subscription is induced by fraud, and is affirmed with knowledge of the fraud, the subscriber cannot maintain an action against the corporation, after insolvency, to recover damages for the deceit; but no authority is cited in support of the decision, and it is contrary to the well-settled rule in the case of contracts generally, that a person who <sup>457</sup> Sherman v. American Stove has been induced to enter into a Co., 85 Mich. 169; Stewart v. Ruth-contract by the fraud of the other party may affirm the contract, and mond & Harrisonburg Land Co., 89 sue to recover damages for the who made or are responsible for the representations,460 or Or he may set up such damages by way of against both.461 counterclaim in an action on the subscription.462

The fact that the corporation has become insolvent, and has made an assignment for the benefit of creditors, does not bar an action against it to recover damages for the deceit, 463 although it may bar the right to rescind the subscription.464

#### § 473. Limitations upon the right to rescind.

(a) In general.—A contract of subscription induced by fraud, like other contracts induced by fraud, is not absolutely void, but merely voidable at the option of the subscriber on discovery of the fraud, or within a reasonable time afterwards, and the subscriber, therefore, may ratify the same, or lose his right to rescind by laches or by the intervention of superior equities of third persons.465

L. 873; Clarke v. Dickson, 6 C. B. (N. S.) 453; Derry v. Peek, 14 App. Cas. 337; Tyler v. Savage, 143 U. S. 79; Dorsey Machine Co. v. Mc-Caffrey, 139 Ind. 545, 47 Am. St. Rep. 290; Miller v. Barber, 66 N. Y. 558; Brewster v. Hatch, 122 N. Y. 349, 19 Am. St. Rep. 498; Paddock v. Fletcher, 42 Vt. 389; Hubbard v. Weare, 79 Iowa, 678; Hornblower v. Crandall, 7 Mo. App. 220, 78 Mo. 581; and cases hereafter cited.

If the directors of a corporation make false and fraudulent representations, in a prospectus or otherwise, for the purpose of inducing the public to subscribe for or purchase shares of its stock, they are all equally liable in an action of deceit to any person who subscribes or purchases shares in reliance on the subscription, and is thereby defrauded. Bagshaw v. Seymour, 93 E. C. L. 873; Bedford v. Bagshaw, 4 Hurl. & N. 538; Clarke v. Dickson, 6 C. B. (N. S.) 453; Watson v. Earl of Charlemont, 12 Q. B. 856. And see post, chapter xxiv.

460 Bagshaw v. Seymour, 93 E. C. cers are not liable in damages because of the fraud of other directors or officers, or of their agents. In re Denham, 25 Ch. Div. 752; Weir v. Barnett, 3 Exch. Div. 32; Mabey v. Adams, 3 Bosw. (N. Y.)

> But if a director acquiesces in false representations by the other directors, it is equivalent to active participation on his part. Vreeland v. New Jersey Stone Co., 29 N. J. Eq. 188.

> As to the liability of a trust company acting as agent of a corporation in selling and issuing certificates of stock, see McClure v. Central Trust Co., 28 App. Div. (N.

> 461 Dorsey Machine Co. v. Mc-Caffrey, 139 Ind. 545, 47 Am. St. Rep. 290.

462 Owens v. Boyd Land Co., 95

463 Dorsey Machine Co. v. Mc-Caffrey, 139 Ind. 545, 47 Am. St. Rep. 290.

464 See post, § 472(g). 465 Oakes v. Turquand, L. R. 2 H. L. 325; Tennent v. City of Glasgow Innocent directors or other offi- Bank & Liquidators, 4 App. Cas.

(b) Ratification as a bar to rescission.—It follows that a ratification or affirmance of the contract of subscription, with knowledge of the fraud, while it does not bar an action of deceit,\* is a complete and absolute bar to a rescission. And such ratification or affirmance may be implied from the acts of the subscriber after discovery of the fraud. If, with full knowledge of the fraud, he acts as a shareholder in the organization of the corporation, or takes part in stockholders' meetings after organization, or acts as an officer, or pays assessments, or receives dividends, or transfers the stock, or does any other act which is inconsistent with an intention to rescind his subscription, he will be held to have ratified the same, and he cannot afterwards rescind, either as against the corporation, or as against its receiver, assignee, or creditors.

In order that acts of a subscriber may amount to a ratification, so as to bar a rescission for fraud, they must have been done with knowledge of the fraud.<sup>468</sup> And they must be incon-

615; Howard v. Turner, 155 Pa. St. 349, 35 Am. St. Rep. 883; and other cases cited in the notes following.

\*See supra, this section, (c). Compare Wilson v. Hundley, 96 Va. 96, referred to in note 459, spra.

<sup>466</sup> Ex parte Briggs, L. R. 1 Eq. 483; City Bank of Macon v. Bartlett, 71 Ga. 797; Marten v. Paul O. Burns Wine Co., 99 Cal. 355; Chaffin v. Cummings, 37 Me. 76; Southern Life Insurance & Trust Co. v. Lanier, 5 Fla. 110, 58 Am. Dec. 448; Wilson v. Hundley, 96 Va. 96; Franey v. Wauwatosa Park Co., 99 Wis. 40; and other cases in the notes following.

467 Ex parte Briggs, L. R. 1 Eq. 483; In re Dunlop-Truffault Cycle & Tube Manufacturing Co., 75 Law T. (N. S.) 385; Marten v. Paul O. Burns Wine Co., 99 Cal. 355; City Bank of Macon v. Bartlett, 71 Ga. 797; Lear v. Paige Lumber & Manufacturing Co. (Tenn.) 42 S. W. 808; Chaffin v. Cummings, 37 Me. 76; Foley v. Holtry, 41 Neb. 563; Franey v. Wauwatosa Park Co., 99 Wis. 40.

A subscriber cannot rescind for fraud of the president, where, for two months after discovery of the fraud, he remains a director, demands his salary as superintendent, and sues the president personally for his damages. Lear v. S. K. Paige Lumber & Mfg. Co. (Tenn. Ch. App.) 42 S. W. 808.

A person cannot rescind a subscription or purchase for fraud, where it appears that on the day he discovered the fraud he attended a stockholders' meeting, and voted for an assessment on the stock, and afterwards, before attempting to rescind, attended another meeting, and voluntarily paid the assessment on his shares. Marten v. Paul O. Burns Wine Co., 99 Cal. 355.

468 Strong v. Southwestern Bridge & Iron Co. (Tex.) 38 S. W. 546; National Bank of Dakota v. Taylor, 5 S. D. 99.

Where a person, who has been induced to subscribe for stock by false representations that certain others have subscribed, affirms the subscription on discovery that the

sistent with an intention to repudiate the contract.469 late Maryland case, a subscriber who had paid part of his subscription before discovery that the prospectus of the corporation, upon reliance on which he had subscribed, contained false and fraudulent representations, repudiated the subscription on discovery of the fraud, but afterwards gave one of the directors a check to aid in saving the property of the corporation. At the time he gave the check, he expressly stated that he would give nothing on his subscription, and that he gave the check merely to save what he had already paid. It was held that the payment, since it was not on account of the subscription, was not a ratification of the subscription, and did not prevent him from setting up the fraud in an action by the trustee of the corporation to recover on the subscription for the benefit of its creditors.470

- (c) Return of stock.—Rescission of a subscription because of false and fraudulent representations ordinarily includes the duty to return or offer to return the certificate of stock if the subscriber has received one from the corporation.<sup>471</sup> But there is no necessity to return or offer to return the certificate if, at the time the fraud is discovered, a note given in part payment of the subscription has been transferred by the corporation and the stock is of no value.472
- (d) Laches as a bar to rescission.—A subscriber cannot rescind his subscription for fraud, either in equity or at law, if he has been guilty of laches, either in repudiating his subscription after discovery of the fraud, or in discovering the fraud. 473

al, he cannot afterwards rescind Neb. 124. on discovering the terms of the option, since these are mere incidents of the fraud, which was known at the time of the affirm-Wilson v. Hundley, 96 Va.

latter's subscriptions were option- ing & Loan Ass'n v. Cameron, 48

472 Zang v. Adams, 23 Colo. 408, 58 Am. St. Rep. 249.

473 Ashley's Case, L. R. 9 Eq. 263; Central Ry. Co. of Venezuela v. Kisch, L. R. 2 H. L. 99; In re London & Staffordshire Fire Ins. 469 Fear v. Bartlett, 81 Md. 435. Co., 24 Ch. Div. 149; Weisiger v. 470 Fear v. Bartlett, 81 Md. 435. Richmond Ice Machine Co., 90 Va. 471 Francis v. New York & Brook- 795; Howard v. Turner, 155 Pa. St. Iyn Elevated R. Co., 108 N. Y. 93; 349, 35 Am. St. Rep. 883; City Zang v. Adams, 23 Colo. 408, 58 Bank of Macon v. Bartlett, 71 Ga. Am. St. Rep. 249. And see Build- 797; Philadelphia, Wilmington & "A man," said Lord Romilly in a leading English case, "must not play fast and loose; he must not say, 'I will abide by the company, if successful, and I will leave the company if it fails; and therefore, whenever a misrepresentation is made of which any one of the shareholders has notice, and can take advantage to avoid his contract with the company, it is his duty to determine at once whether he will depart from the company, or whether he will remain a member."474

Whether a subscriber's delay in rescinding his subscription for fraud was unreasonable, so as to constitute laches, depends upon the circumstances, as well as upon the extent of the delay. Even a long delay will not be fatal if satisfactorily explained, and if the circumstances are not such as to render rescission inequitable.475

The burden of showing knowledge of the fraud and failure to rescind is on the corporation.476

B. R. Co. v. Cowell, 28 Pa. St. 329, 70 Am. Dec. 128; Marten v. Paul O. Burns Wine Co., 99 Cal. 355; Upton v. Englehart, 3 Dill. 496, Fed. Cas. No. 16,800; Farrar v. Walker, 3 Dill. 506, note, Fed. Cas. No. 4,-679; Upton v. Jackson, 1 Flip. 413, Fed. Cas. No. 16,802; Zang v. Adams, 23 Colo. 408, 58 Am. St. Rep. 249; Ross-Meehan Brake Shoe Foundry Co. v. Southern Malleable Iron Co., 72 Fed. 957; Newton Nat. Bank v. Newbegin, 40 U. S. App. 1, 74 Fed. 135; Schanck v. Morris, 7 Rob. (N. Y.) 658; Fey v. Peoria Watch Co., 32 Ill. App. 618; Dynes v. Shaffer, 19 Ind. 165; State v. Jefferson Turnpike Co., 3 Humph. (Tenn.) 305; Cedar Rapids Ins. Co. v. Butler, 83 Iowa, 124; American Building & Loan Ass'n v. Rainbolt, 48 Neb. 434; Duffield v. E. T. Barnum Wire & Iron Works, 64 Mich. 293; Northrop v. Bushnell, 38 Conn. 498; Barrows v. Natchaug Silk Co., 498; Barrows v. Natchaug Silk Co., 72 Conn. 658; Bartol v. Walton & v. Kisch, L. R. 2 H. L. 99; McClel-Whann Co., 92 Fed. 13; Urner v. lan v. Scott, 24 Wis. 81; Zang v. Sollenberger, 89 Md. 316; Tierney Adams, 23 Colo. 408, 58 Am. St. v. Parker, 58 N. J. Eq. 117; Martin v. South Salem Land Co., 94 [1896] App. Cas. 273. Va. 28. And see In re Dunlop-Truffault Cycle & Tube Mfg. Co. App. Cas. 273; Virginia Land Co.

(Ex parte Shearman) 66 Law J. Ch. 25, 75 Law T. (N. S.) 385.

A subscriber cannot rescind for fraud where he has accepted dividends and participated in stockholders' meetings for a number of years, without investigating as to the truth of the alleged false representations, and an investigation might have easily been made by examining the books of the corporation. Barrows v Silk Co., 72 Conn. 658. Barrows v. Natchaug

One who has been induced by fraud to subscribe for stock is not affected with knowledge of the fraud by the disclosure of facts at a stockholders' meeting for which the perpetrator of the fraud holds proxies for him, and at which he is not present. Virginia Land Co. v. Haupt, 90 Va. 533, 44 Am. St. Rep. 939.

474 Ashley's Case, L. R. 9 Eq. 263. 475 Central Ry. Co. of Venezuela

- (e) Removal of name from books.—In the absence of statutory provision to the contrary, all that is necessary, in order that a subscriber may effectually avoid his subscription on the ground of fraud, is that he shall seasonably repudiate the same, and notify the company of the repudiation; and he is under no duty to see that his name is removed from the books of the company,477
- (f) Rescission as against third persons.—When a negotiable note is given in payment of a subscription for stock, and the subscription is afterwards rescinded for fraud, the note cannot be avoided in the hands of a bona fide purchaser for value. But it may be avoided in the hands of one who was not a purchaser for value, or who purchased with notice of the fraud.473
- (g) Effect of insolvency of the corporation.—All the courts agree, no doubt, that the fact that a corporation is insolvent, and that an action on a subscription is brought by its receiver or assignee for the benefit of creditors, or by creditors themselves, where this is allowed, cannot affect the subscriber's right to set up as a defense that the subscription was induced by fraud, if he repudiated the subscription before the corporation's insolvency, and while it was a going concern. 479 This does not conflict with the doctrine known as the "trust fund doctrine,"—that the assets of a corporation, when it is insolvent, constitute a trust fund for the payment of its debts.480

"Whatever may have been the origin of the doctrine," said the Maryland court in a late case, "it means and can only mean, that when a corporation has been lawfully dissolved or has become insolvent, its entire property, including unpaid subscriptions to its capital stock, becomes a trust fund for the payment

Rep. 939.

<sup>477</sup> Savage v. Bartlett, 78 Md.

<sup>478</sup> Zang v. Adams, 23 Colo. 408. 58 Am. St. Rep. 249.

<sup>479</sup> Savage v. Bartlett, 78 Md. Co., 62 Law T. (N. S.) 791; Ten-561; Fear v. Bartlett, 81 Md. 435; nent v. City of Glasgow Bank & Central Ry. Co. of Venezuela v. Liquidators, 4 App. Cas. 615. Kisch, L. R. 2 H. L. 99; Reese Riv-

v. Haupt, 90 Va. 533, 44 Am. St. er Silver Mining Co. v. Smith, L. R. 4 H. L. 64; Ramsey v. Thompson Mfg. Co., 116 Mo. 313; Cocksedge v. Metropolitan Coal Consumers' Ass'n 64 Law T. (N. S.) 826.

Compare In re Lenox Publishing

of its debts, and that creditors are entitled in equity to have their debts paid out of the assets of the company before there can be any distribution among the stockholders. And no one can question the justice and sound sense of the doctrine as thus understood. But it is only when the company has been dissolved or has become insolvent that this equitable doctrine arises. So long as the company is a going concern, having the possession and management of its property, contracts made by and with the company are governed by the same principles of law as contracts between individuals. And such being the case, if one is induced to become a subscriber to its capital stock by the fraud of the company and within a reasonable time after the discovery of the fraud, there being no laches on his part in discovering the fraud, repudiates his subscription, and this, too, before the insolvency of the company, under such circumstances he is, according to the settled law of this country, relieved of all liability on account of his subscription. relieved because he has the right to avoid a fraudulent contract, and because he has exercised this right. The subsequent insolvency of the company can upon no principle make him liable on a fraudulent contract which he has thus repudiated. And under such circumstances we cannot agree that the equities of the creditor are superior to those of the defrauded shareholder. And when we speak of the right of the defrauded shareholder to rescind his contract before the insolvency of the company, we mean before proceedings in insolvency voluntary or involuntary have been instituted, or some act done that in law is regarded as an act of insolvency, for until then the trustfund doctrine relied on by the appellee has no application."481

In England, and in some of the states in this country, it has been held that a subscription cannot be repudiated on the ground of fraud, for the first time, after the corporation has become insolvent, and has made an assignment or gone into the hands of a receiver or an assignee in bankruptcy, even though the fraud may not have been discovered before insolvency, and

<sup>481</sup> Fear v. Bartlett, 81 Md. 435.

though there may have been no laches in discovering it.482 According to the better opinion, however, this doctrine cannot be sustained without qualification. Surely, the equity of a person who has been induced to subscribe for stock in a corporation, without negligence on his part, by the deceit of its officers or agents, and who has not been guilty of negligence, either in failing to discover the fraud, or in repudiating his subscription after its discovery, cannot be said to be inferior to the equity of persons dealing with the corporation and becoming its creditors, and he should not be denied the right to set up the fraud as a defense in an action or other proceeding to enforce his subscription, merely because the corporation has become insolvent, and it is sought to enforce the subscription for the benefit of its The view that he has such right is supported by wellcreditors. considered cases, both in England and in this country. 483 rule should undoubtedly be applied where no debts have been contracted by the corporation since the date of the subscription.484

In all jurisdictions, no doubt, insolvency of the corporation will bar rescission of a subscription on the ground of fraud, where there have been laches, either in electing to rescind after discovery of the fraud or in discovering the fraud.485

482 Oakes v. Turquand, L. R. 2 H.
L. 325; Wright's Case, L. R. 12 commenced after commencement Eq. 331; Kent v. Freehold Land & of winding-up proceedings, where Brick-Making Co., L. R. 3 Ch. App.
493; Turner v. Grangers' Life & faith, and in ignorance of the wind-Health Ins. Co., 65 Ga. 649; Howard v. Glenn, 85 Ga. 238, 21 Am.
St. Rep. 156; Howard v. Turner, St. Rep. 156; Howard v. Turner, St. Rep. 283; Duffield v. Barnum Wire & Mining Co., 3 Ch. Div. 749; Ramston Works, 64 Mich. 293; Bissell v. Thompson Mfg. Co., 116 Mo. 313; Robinson v. Dickey, 14 Tex. Civ. App. 700; Beal v. Dillon, 5 v. Heath, 98 Mich. 472; Olson v. State Bank, 67 Minn. 267; McDowall v. Sheehan, 13 N. Y. Supp. 386. In case of bankruptcy proceed-

ings, see Michener v. Payson, 13 N. Bank, 66 Fed. 701; Savage v. Bart-B. R. 49, Fed. Cas. No. 9,524; Farlett, 78 Md. 561; Fear v. Bartlett, rar v. Walker, 13 N. B. R. 82, 81 Md. 435. Fed. Cas. No. 4,679.

where proceedings to rescind a sub- gheny Geometrical Wood Carving

In case of bankruptcy proceed- affirming Newbegin v. Newton Nat.

484 Beal v. Dillon, 5 Kan. App. 27. Compare Hall v. Old Talargoch

485 Chubb v. Upton, 95 U. S. 665,
Lead Mining Co., 3 Ch. Div. 749, and cases cited; Hilliard v. AlleInsolvency of the corporation does not bar an action by a subscriber against the corporation and its assignee to recover damages for fraud inducing the subscription.<sup>486</sup>

- V. WITHDRAWAL, RELEASE, AND DISCHARGE OF SUBSCRIBERS.
- § 474. In general.—After a subscription has become a binding contract, the subscriber cannot surrender his shares and withdraw, so as to avoid further liability on his subscription, without the consent of the corporation, unless he has the right to do so under valid special terms of his contract. But he may be released by the corporation, or discharged from liability, as follows:
- (1) He cannot be released by the corporation from liability on his subscription, otherwise than by a bona fide compromise, without the consent of all the other stockholders. Nor can he be released with the consent of all the other stockholders to the prejudice of creditors of the corporation. He may be released, however, with the consent of all the stockholders, if there is no fraud upon creditors. And he may be released by virtue of a bona fide compromise without the consent of other stockholders, and as against creditors.
- (2) He may be discharged from liability by a valid and full payment of his subscription.
- (3) Or, in most jurisdictions, although not in all, by a bona fide transfer of his shares.
- (4) Or by a discharge in bankruptcy, where the subscription is due at the time of the discharge.
- (5) Or by a material alteration of his contract, without his consent.
- (6) Or by nonperformance by the corporation of conditions precedent in the contract, or, under some circumstances, of special terms.
- (7) By a material or fundamental alteration or amendment of the charter of the corporation, without his consent.
  - (8) By a consolidation of the corporation with another, without

Co., 173 Pa. St. 1; Howard v. Turleable Iron Co., 72 Fed. 957; Safner, 155 Pa. St. 349, 35 Am. St. fold v. Barnes, 39 Miss. 399; Rug-Rep. 883; Martin v. South Salem gles v. Brook, 6 Hun (N. Y.) 164; Land Co., 94 Va. 28; Duffield v. E. Northrop v. Bushnell, 38 Conn. 498. T. Barnum Wire & Iron Works, 64 Mich. 293; Ross-Meehan Brake Caffrey, 139 Ind. 545, 47 Am. St. Shoe Foundry Co. v. Southern Mal-Rep. 290.

his consent, where the consolidated corporation is of a different character, or has materially different powers.

- (9) But he is not discharged by special agreements of the corporation with, or release of, or nonpayment by, other stockholders.
- (10) Nor by any act of the corporation which is within the powers conferred upon it by its charter.
  - (11) Nor by mismanagement of the corporation.
- (12) Nor by the fact that it has failed to perform conditions subsequent prescribed by its charter or the general law, or has violated its charter, or engaged in ultra vires or illegal acts, so that its charter is subject to forfeiture in proceedings by the state.
- (13) Nor by nonuser of its franchises, unless there has been an abandonment of the enterprise, and there are no debts to be paid.
- (14) He is not discharged by mere delay in enforcing the subscription unless an action is barred by the statute of limitations. The statute begins to run when the subscription is payable and a right of action accrues. By the weight of authority, this is not until a valid call is made, when a call is necessary.

### § 475. Withdrawal of subscribers.

A subscriber for stock in a corporation may revoke his offer and withdraw, or the offer may lapse by reason of his death, etc., at any time before the subscription has been accepted by the corporation, unless the subscription is binding, prior to its acceptance, by virtue of some statute; for until acceptance there is no contract binding upon the corporation, and unless both the subscriber and the corporation are bound, neither is bound.487 It is otherwise, however, after a subscription has been accepted by the corporation, and become a binding contract. In such a case, the subscriber cannot withdraw or surrender his shares, or substitute another contract, or another subscriber, and thereby avoid liability on his subscription as made, without the consent of the corporation,488 unless he is given the right to withdraw

<sup>487</sup> Hudson Real Estate Co. v. Tower, 156 Mass. 82, 32 Am. St. Tipton, 5 Ala. 787, 59 Am. Dec. 344; Rep. 434, 161 Mass. 10, 42 Am. St. Busey v. Hooper, 35 Md. 15, 6 Am. Rep. 379; Bryant's Pond Steam Rep. 350; Hutchins v. Smith, 46 Mill Co. v. Felt, 87 Me. 234, 47 Am. Barb. (N. Y.) 235; Armstrong v. St. Rep. 323. And see ante, § 451. Karshner, 47 Ohio St. 276; Muskin-

by valid special terms of his contract. 489 Nor can he do so, as a general rule, even when the corporation consents, if any of the other stockholders object, or if there is any prejudice to cred-This is true in the case of subscriptions upon conditions precedent, as well as in the case of subscriptions which are absolute and unconditional.491

A subscriber may be given the right to return his stock and withdraw by the special terms of his contract, provided the agreement does not operate as a fraud upon other subscribers, or upon creditors of the corporation, but not otherwise. 492 And he may rescind his contract and recover what he has paid, subject to limitations elsewhere shown, if the subscription was induced by false and fraudulent representations for which the corporation is responsible. 493 And he may also be entitled to withdraw and be discharged from liability by failure of the corporation to comply with conditions precedent, 494 by a material alteration of his contract of subscription, 495 by a material alteration of the charter of the corporation, 496 etc.

## Release of subscribers by the corporation.

There can be no doubt that a corporation may effectually release a subscriber from liability on his subscription, in whole or

gum Valley Turnpike Co. v. Ward. 13 Ohio, 120, 42 Am. Dec. 191; Klein v. Alton & Sangamon R. Co., 13 Ill. 514; Ryder v. Alton & Sangamon R. Co., 13 III. 516; Bordentown & South Amboy Turnpike Co. v. Imlay, 4 N. J. Law, 285; Gleaves v. Brick Church Turnpike Co., 1 Sneed (Tenn.) 491; Lowe v. Edgefield & K. R. Co., 1 Head (Tenn.) 659; Greenville & Columbia R. Co. v. Coleman, 5 Rich. L. (S. C.) 118; 42 Am. Rep. 548; Cheraw & Chester R. Co. v. White, 10 Rich. (S. C.) 155; Chicago Building & Mfg. Co. v. Lyon (Okla.) 64 Pac. 6.

A majority of the stockholders cannot withdraw. Busey v. Hooper, 35 Md. 15, 6 Am. Rep. 350. 489 See infra, this section.

490 As to whether a corporation may release a subscriber, see post, § 476.

491 Armstrong v. Karshner, 47 Ohio St. 276; Hutchins v. Smith, 46 Barb. (N. Y.) 235; ante, § 461(a).

492 Jones v. Johnson, 86 Ky. 530; Vent v. Duluth Coffee & Spice Co., 64 Minn. 307; Browne v. St. Paul Plow Works, 62 Minn. 90; Winston Jones v. Milton & Rushville Turn- v. Dorsett Pipe & Paving Co., 129 pike Co., 7 Ind. 547; Greer v. Ill. 64, 2 Smith's Cas. 857, 2 Keen-Chartiers Ry. Co., 96 Pa. St. 391, er's Cas. 1212; McComb v. Barceer's Cas. 1212; McComb v. Barcelona Apartment Ass'n, 134 N. Y. 598; Railway Co. v. Fisher, 39 Ohio St. 330. And see ante, § 467.

<sup>493</sup> Ante, § 468 et seq.

494 Post, § 481; ante, § 455 et seq.

495 Post, § 480.

496 Post, § 482.

in part, or allow him to modify his contract, if all the stockholders expressly or impliedly consent, and if there is no fraud upon existing or subsequent creditors, 497 provided there is a consideration for the release.498 It is thoroughly well-settled,

497 Cooper v. Frederick, 9 Ala. 738; Glenn v. Hatchett, 91 Ala. 316; Winston v. Dorsett Pipe & Paving Co., 129 Ill. 64, 2 Smith's Cas. 857, 2 Keener's Cas. 1212; Non-Electric Fibre Mfg. Co. v. Peabody, 21 App. Div. (N. Y.) 247; Cusick v. Morgan v. Lewis, 46 Ohio St. 1, 1 Keener's Cas. 697; Gelpcke v. Blake, 19 Iowa, 263; Stuart v. Valley R. Co., 32 Grat. (Va.) 146; Hollingshead v. Woodward, 35 Hun (N. Y.) 410; Nettles v. Marco, 33 S. C. 47; Hill v. Silvey, 81 Ga. 500; Wangerien v. Aspell, 47 Ohio St. 250; Sanderson v. Aetna Iron & Nail Co., 34 Ohio St. 442. See, also, Alling v. Wenzel, 133 Ill. 264; Republic Life Ins. Co. v. Swigert, 135 Ill. 150; Howe Grain & Mercantile Co. v. Jones, 21 Tex. Civ. App. 198.

As to the admissibility and sufficiency of evidence to show a release and cancellation of subscriptions, see Pacific Fruit Co. v. Coon, 107 Cal. 447; Stuart v. Valley R.

Co., 32 Grat. (Va.) 146.

That the directors have no power to release subscribers, unless it is expressly conferred upon them by the charter or statute, or by the stockholders by a by-law or otherwise, see post, chapter xxiv.

The secretary has no such power. Minnehaha Driving Park Ass'n v. Legg, 50 Minn. 333. See post,

chapter xxiv.

Nor can the president. Fuches v. Hamilton Tribune Printing & Publishing Co., 10 Ont. (Can.) 497. See, also, United Growers' Co. v. Eisner, 22 App. Div. (N. Y.) 1. And see post, chapter xxiv.

That another person may be substituted as subscriber by agreement with the corporation, see Weinman v. Wilkinsburg & E. L. Pas- v. Talbot, 131 Cal. 45. senger Ry. Co., 118 Pa. St. 192.

An agreement between a corporation and its stockholders, whereby the latter, who have paid only twenty per cent. of the par value of their stock, may surrender the stock in exchange for full-paid stock to the amount of one-fifth of Bartlett, 91 Me. 153; Shoemaker v. their subscriptions, was held valid Washburn Lumber Co., 97 Wis. as between the parties. Republic 585; Jones v. Johnson, 86 Ky. 530; Life Ins. Co. v. Swigert, 135 Ill. 150.

> Under a statute making stockholders liable for the amount unpaid on their stock, and providing that no assignor of stock shall be released by the assignment, a subscriber for stock, who surrenders it to the corporation after part payment, is not liable to creditors for the balance, where the stock is reissued by the \*corporation, and paid for in full by the purchaser. First Nat. Bank v. Peoria Watch Co., 191 Ill. 128.

If a corporation is not a going concern, and has no creditors or contract obligations, it is competent for its directors, who are its only stockholders, to make an agreement releasing themselves, as stockholders or subscribers, from liability to the corporation or to each other. Non-Electric Fibre Mfg. Co. v. Peabody, 21 App. Div. Non-Electric Fibre (N. Y.) 247.

Where the rights of creditors are not involved, a corporation cannot recover on a subscription for stock, where, with the consent of subscribers, it has sold out its entire authorized stock, including that subscribed for. Level Land Co. v.

Hayward, 95 Wis. 109.

Release of a subscription for stock may be proved as well by the acquiescence of the stockholders, and the fact that the corporation did not regard it as binding, as by its records. Tulare Savings Bank

498 Northrop v. Bushnell,

however, that a corporation cannot, except in pursuance of a bona fide compromise, 499 release a stockholder from liability on his subscription, by accepting a surrender of his shares, or purchasing the same, or otherwise, as against dissenting stockholders, or as against creditors of the corporation. As against them, a release, except as stated above, is void. 500

Div. (N. Y.) 1.

consideration. Zirkel v. Joliet Opera-House Co., 79 Ill. 334.

An agreement between a corporation and a subscriber, who has given his note in payment of his subscription, that in consideration of certain payments on the note it will discharge him from further liability on it, is void for want of consideration. Northrop v. Bushnell, 38 Conn. 498.

499 See infra, this section.

500 Kidwelly Canal Co. v. Raby,
2 Price, 93; Sawyer v. Hoag, 17 Wall. (U. S.) 620, 2 Keener's Cas. 1873, 2 Smith's Cas. 812, 1 Cum. Cas. 818; Potts v. Wallace, 146 U. S. 689; Payne v. Bullard, 23 Miss. 88, 55 Am. Dec. 74; Cartwright v Dickinson, 88 Tenn. 476, 17 Am. St. Rep. 910; Currier v. Lebanon Slate Co., 56 N. H. 262, 1 Keener's Cas. 685; White Mountains R. Co. v. Eastman, 34 N. H. 124; Marshall Foundry Co. v. Killian, 99 N. C. 501, 6 Am. St. Rep. 539; Heggie v. People's Building & Loan Ass'n, 107 N. C. 581; Harmon v. Hunt, 116 N. C. 678; Slee v. Bloom, 19 Johns. (N. Y.) 456; Melvin v. Lamar Ins. Co., 80 Ill. 446, 22 Am. Rep. 199, 2 Smith's Cas. 852, 2 Keener's Cas. 1197; Great Western Telegraph Co. v. Haight, 49 Ill. App. 633; Stone v. Vandalia Coal & Coke Co., 59

Conn. 498. And see Zirkel v. Joliet III. App. 536; Carter v. Union Opera House Co., 79 III. 334; Unit-Printing Co., 54 Ark. 576; Hughes ed Growers' Co. v. Eisner, 22 App. v. Antietam Mfg. Co., 34 Md. 316; Gill v. Balis, 72 Mo. 424; Chouteau An agreement by a corporation, Ins. Co. v. Floyd, 74 Mo. 286; Lake without consideration, to release a Ontario, Auburn & N. Y. R. Co. v. subscriber from liability on his Mason, 16 N. Y. 451; Mann v. subscription, is void, and cannot Pentz, 2 Sandf. Ch. (N. Y.) 257; be set up to defeat an action by the Balfour v. Baker City Gas Co., 27 corporation to enforce the sub- Or. 300; Jewett v. Valley Ry. Co., scription. A plea of release by a 34 Ohio St. 601; Boney v. Williams, subscriber must allege or show a 55 N. J. Eq. 691; Johnson v. Waconsideration. Zirkel v. Joliet Opbash & Mt. Vernon Plank-Road Co., 16 Ind. 389; Bedford R. Co. v. Bowser, 48 Pa. St. 29; United Society v. Eagle Bank of New Haven, 7 Conn. 456; Bishops' Fund v. Eagle Bank of New Haven, 7 Conn. 476; Pacific Fruit Co. v. Coon, 107 Car. 447; Farnsworth v. Robbins, 36 Minn. 369; Vick v. La Rochelle, 57 Miss. 602; Northrop v. Bushnell, 38 Conn. 498; World's Fair E. & T. Boat Co. v. Gasch, 162 Ill. 402; Vance & Jones Co. v. Bentley, 92 Ill. App. 287; Bouton v. Dement, 123 Ill. 142; Swartwout v. Michigan Air Line R. Co., 24 Mich. 389; Osgood v. King, 42 Iowa, 478; Nichols v. Stevens, 123 Mo. 96, 45 Am. St. Rep. 514; Gogebic Invest-ment Co. v. Iron Chief Mining Co., 78 Wis. 427, 23 Am. St. Rep. 417; Hall v. Henderson, 126 Ala. 449.

"The governing officers of a corporation cannot, by agreement or other transaction with the stock-holders, release the latter from their obligation to pay, to the prejudice of creditors, except by fair and honest dealing, and for a valuable consideration." Mr. Justice Miller, in Sawyer v. Hoag, 17 Wall. (U. S.) 620, 2 Keener's Cas. 1873, 2 Smith's Cas. 812, 1 Cum. Cas. 818.

That subsequent creditors cannot

The doctrine invalidating the release of a subscriber by the corporation as against dissenting stockholders and creditors does not prevent a bona fide compromise between a corporation and a subscriber. If a stockholder is unable to pay for his shares, and the transaction is in good faith, the corporation may accept a surrender of his shares and release him from any further liability.<sup>501</sup> The surrender of the shares under such circumstances is not inconsistent with the doctrine recognized in some jurisdictions, 502 that a corporation cannot deal in or purchase its own shares. The surrender, said Lord Herschell in an English case, like a forfeiture, "does not involve any payment out of the funds of the company. If the surrender were made in consideration of any such payment it would be neither more nor less than a sale, and open to the same objections. If it were accepted in a case when the company were in a position to forfeit the shares, the transaction would seem to be perfectly valid." 503

Nor does the general rule apply when there is a bona fide dispute as to liability on a subscription. In such a case, the corporation, if the transaction is in good faith, may compromise the dispute, accepting a surrender of his shares from the subscriber, and releasing him from further liability.<sup>504</sup>

burn Lumber Co., 97 Wis. 585.

A by-law of a corporation allowing stockholders to surrender their shares and withdraw by giving notice, and providing for payment to them of the value of their shares, is illegal, where a statute prohibits withdrawal by stockholders of any part of the capital stock except on discolution. Vercoutere v. Golden State Land Co., 116 Cal. 410. Indeed, such a by-law is illegal, even in the absence of such an express prohibition, as against creditors of the corporation. See the cases cited supra, in this note. Compare Howe Grain & Mercantile Co. v. Jones, 21 Tex. Civ. App. 198. 501 Trevor v. Whitworth, 12 App. Cas. 409, 1 Keener's Cas. 694, 2

Smith's Cas. 977, 1 Cum. Cas. 384; Hope v. International Financial

complain, see Shoemaker v. Wash- Society, 4 Ch. Div. 327; New Haven Trust Co. v. Gaffney, 73 Conn. 480. Compare Hill v. Atoka Coal & Mining Co. (Mo.) 21 S. W. 508. 502 Ante, § 199 et seq.

503 Trevor v. Whitworth, 12 App. Cas. 409, 1 Keener's Cas. 694, 2. Smith's Cas. 977, I Cum. Cas. 384. 504 New Albany v. Burke, 11 Wall. (U. S.) 96; Whitaker v. Grummond, 68 Mich. 249; Berks & Dauphin Turnpike Road v. Myers, 6 Serg. & R. (Pa.) 12, 9 Am. Dec. 402; Philadelphia & West Chester R. Co. v. Hickman, 28 Pa. St. 318; State v. Oberlin Building & Loan Ass'n, 35 Ohio St. 258, 1 Keener's Cas. 405, 1 Smith's Cas. 375, 1 Cum. Cas. 566; Morgan v. Lewis, 46 Ohio St. 1, 2 Keener's Cas. 697; Gelpcke v. Blake, 19 Iowa, 263; New Haven Trust Co. v. Gaffney, 73 Conn. 480. There must be a compromise.

Nor does the rule prevent a corporation which is indebted to a subscriber from canceling the subscription by setting off its indebtedness, for a corporation may contract with its stockholders, and pay debts due from it to them, as it may pay its other debts, provided there is no fraud upon other creditors. 505

There is nothing to prevent an agreement between a subscriber and other stockholders as individuals, by which the latter agree to purchase his shares from him. This is not in any sense a release of the subscriber by the corporation, and is not fraudulent as against other subscribers.506

#### Discharge by payment. § 477.

Of course a subscriber is discharged from further liability on his subscription by full payment of the same, although by virtue of a provision in the charter or general law he may be subject to further assessment for the payment of the debts of the corporation, or for the purposes of the corporation itself. 507 The only difficulty in this connection is in determining what constitutes payment. As we have elsewhere seen, payment may be made in property, labor, or services, or in bonds, notes, mortgages, or any other equivalent of money, unless this is prohibited, expressly or impliedly, by some charter, statutory, or constitutional provision. 508 We have also seen that a payment of less than the par value of stock, while it may be a good discharge as against the corporation and consenting stockholders, will generally be no discharge as against dissenting stockholders and creditors of the corporation. This subject has been very fully dealt with in a former chapter.

#### § 478. Discharge by transfer of shares.

By the weight of authority, in the absence of statutory provision to the contrary, a subscriber and stockholder who has made

238, 21 Am. St. Rep. 156. 505 Goodwin v. McGehee, 15 Ala.

232. And see ante, § 386.

506 Morgan v. Struthers, 131 U.

and not a mere offer to compro-S. 246; Traphagen v. Sagar, 63 mise. Howard v. Glenn, 85 Ga. Minn. 317; Meyer v. Blair, 109 N. 507 Ante, §§ 402-404.
508 Ante, §§ 380-386.
509 Ante, §§ 389-401.

a bona fide sale and transfer of his stock, and in doing so complied with the requirements of the charter and by-laws of the corporation, is no longer under any liability on the subscription except for assessments or calls made prior to the transfer. The transferee takes his place with respect both to the rights and to the liabilities attaching to the shares. This doctrine, however, has not been recognized in all the states, even in the absence of a statute, and in some states statutes have been enacted making the transferrer of shares liable for any balance due on his subscription, notwithstanding the transfer. The question will be fully considered in treating of the transfer of shares.<sup>510</sup>

# § 479. Discharge in bankruptcy.

A valid discharge in bankruptcy discharges the debtor from liability upon subscriptions for stock made prior to the discharge, as well as from other debts, if liability on the subscription existed prior to the discharge.<sup>511</sup>

## § 480. Discharge by alteration of contract.

It is a general principle that a material alteration of a written contract by one of the parties, or by a stranger with his consent, without the consent of the other party, even when the alteration is made without any fraudulent intent, discharges the other party from liability on the contract as originally made; and of course he cannot be held liable on the contract as altered, since he has never consented thereto. The principle applies with full force to a contract of subscription. If, therefore, a subscription

510 See post, § 557 et seq.
 511 Glenn v. Abell, 39 Fed. 10;
 Carey v. Mayer (C. C. A.) 79 Fed.
 926.

The obligation of a subscriber to repond to calls becomes a liability with a contingency, although not fixed in amount, nor payable until a call has been made, upon the declared insolvency of the corporation by execution of a deed of trust for the benefit of creditors; and if he files a petition in bankruptcy after the execution of the 40.

deed of trust, and is discharged, the discharge releases him from liability on the subscription, although no call may have been made until after the discharge. Carey v. Mayer (C. C. A.) 79 Fed.

Contra, where a call was necessary, and had not been made. Sayre v. Glenn, 87 Ala. 631; Lehman v. Glenn, 87 Ala. 618; Semple v. Glenn, 91 Ala. 245, 24 Am. St. Rep. 894; Glenn v. Howard, 65 Md. 40

paper, or articles of association in which subscriptions are made, is materially and intentionally altered without the consent of a party thereto, by the corporation or its agent, or by a stranger with its consent, his subscription cannot be enforced.<sup>512</sup> A subscriber who signs articles of association is not liable on his subscription if the articles are materially altered by the corporation or the corporators, or new articles substituted, without his consent.513

Immaterial changes in the contract of subscription or articles of association will not operate as a discharge.<sup>514</sup> And of course an alteration of a subscription paper may always be explained. It will not operate as a discharge if it was due to accident or mistake, or if made by a stranger without the consent of the corporation, or by the corporation with the consent of the subscriber.515

### Discharge by nonperformance of conditions precedent or § 481. special terms.

When a subscription is made upon a condition precedent, the condition must be performed before the subscriber can be held liable on his subscription, unless he waives the condition, or is estopped, and if there is a breach of the condition, he is dis-

512 Burrows v. Smith, 10 N. Y. list. Sodus Bay & Corning R. Co. 550; Bery v. Marietta, Pittsburgh v. Hamlin, 24 Hun (N. Y.) 390. & C. Ry. Co., 26 Ohio St. 673; Richmond St. R. Co. v. Reed, 83 Ind. the corporation does not relieve 9; Southern Hotel Co. v. Newman, 30 Mo. 118; Katama Land Co. v. Jernegan, 126 Mass. 155; Jackson v. Cherokee Medicine Co., 47 S. C. 215; Texas Printing & Lithographing Co. v. Smith (Tex. App.) 14 S. W. 1074.

518 Richmond St. R. Co. v. Reed, 83 Ind. 9; Burrows v. Smith, 10 N. Y. 550; Southern Hotel Co. v. Newman, 30 Mo. 118.

514 Union Agricultural & Stock Ass'n v. Neill, 31 Iowa, 95.

Where a number of similar subscriptions are made on separate lists, it is not a material alteration to cut and paste them all under one heading, so as to make one Y.) 56.

stockholders from liability. Priest v. Glenn, 4 U. S. App. 478, 51 Fed. 400; Glenn v. Springs, 26 Fed. 494; Howard v. Glenn, 85 Ga. 238, 21 Am. St. Rep. 156; Bucksport & Bangor R. Co. v. Buck, 68 Me. 81; Haskell v. Sells, 14 Mo. App. 91; Haskell v. Worthington, 94 Mo. 560; Delaware & Atlantic R. Co. v. Irick, 23 N. J. Law, 321; Green-ville & P. R. Narrow Gauge R. Co. v. Johnson, 8 Baxt. (Tenn.) 332; Racine County Bank v. Ayres, 12 Wis. 512.

515 Johnson v. Wabash & Mt. Vernon Plank Road Co., 16 Ind. 389; Rensselaer & Washington Plank Road Co. v. Wetsel, 21 Barb. (N.

charged from his contract.<sup>516</sup> He is discharged, in the absence of a waiver or estoppel, if the condition is not performed within the time, if any, specified in the contract, or within a reasonable time, if no time is specified. 517

If a subscription is not upon a condition precedent, but upon special terms, and the special terms constitute a mere independent and collateral undertaking on the part of the corporation, failure of the corporation to perform such special terms will not generally operate to discharge the subscriber from liability on his subscription, but his remedy is by an action or counterclaim against the corporation to recover damages for its breach of contract.<sup>518</sup> If the special term, however, or undertaking on the part of the corporation, forms substantially the whole consideration for the subscription, a breach thereof by the corporation before the subscription is paid will discharge the subscriber, except as against creditors, on the ground that there is a failure of consideration. Where a landowner subscribed for stock in a turnpike company, in consideration of the company's promise to run its road along a certain route, and, before the subscription was paid in full, the road was laid out along a different route, so as to "subvert and destroy the consideration" which induced the subscription, it was held that the subscriber was discharged, and that he could maintain a suit in equity to enjoin the company from collecting a judgment for assessments on the subscription recovered prior to the breach, and to recover assessments which he had paid.519

There are many other cases in which subscribers for stock in railroad and turnpike companies upon condition or stipulation

516 Ticonic Water Power & Mfg. 48 Neb. 434. And see ante, §§ 457, Co. v. Lang, 63 Me. 480; Martin v. 465, 466. Pensacola & Georgia R. Co., 8 Fla. 519 Frankfort & Shelbyville Turn-370, 73 Am. Dec. 713. And see pike Co. v. Churchill, 6 T. B. Mon. ante, § 455 et seq.

517 Ticonic Water Power & Mfg. Co. v. Lang, 63 Me. 480; Hutchins v. Smith, 46 Barb. (N. Y.) 235. See ante, § 461(c).

Parks, 86 Tenn. 554; American and refuses to elect him superin-Building & Loan Ass'n v. Rainbolt. tendent, he may tender back the

(Ky.) 427, 17 Am. Dec. 159. See, also, Caley v. Philadelphia & Chester County R. Co., 80 Pa. St. 363.

Where a corporation sells stock on credit under an agreement that the purchaser shall be elected its 518 Paducah & Memphis R. Co. v. superintendent at a certain salary. that the road should be constructed along a certain route, or between certain termini, have been allowed to defeat a recovery on their subscriptions by setting up the defense that the company failed to construct the road as agreed, or afterwards changed its location.<sup>520</sup> The same is true of subscriptions for stock in a bridge company, where the company changes the location of the bridge,<sup>521</sup> and of a contract of subscription for stock in a manufacturing company, the articles of association of which require its plant to be located at a particular place, and which establishes the same at a different place.<sup>522</sup>

It is no defense to an action on a subscription that the corporation has guarantied to pay interest on stock "as soon as paid,"

stock, and recover what he has paid on it. Seymour v. Detroit Copper & Brass Rolling Mills, 56 Mich. 117.

Champion v. Memphis & Charleston R. Co., 35 Miss. 692; Noesen v. Town of Port Washington, 37 Wis. 168; Rensselaer & Washington Plank Road Co. v. Wetsel, 6 How. Pr. (N. Y.) 68; Buffalo & Jamestown R. Co. v. Gifford, 87 N. Y. 294; Buffalo, Corning & N. Y. R. Co. v. Pottle, 23 Barb. (N. Y.) 21; Caley v. Philadelphia & Chester County R. Co., 80 Pa. St. 363; Moore v. Hanover Junction & Susquehanna R. Co., 94 Pa. St. 324; Nashville & Northwestern R. Co. v. Jones, 2 Cold. (Tenn.) 574. Compare Russell v. Alabama Midland R. Co., 94 Ga. 510; Central Plankroad Co. v. Clemens, 16 Mo. 359; White Hall & Plattsburg R. Co. v. Myers, 16 Abb. Pr. (N. S.; N. Y.) 34.

Mere intention on the part of the corporation to depart from the route laid out in the charter is no defense. Ex parte Booker, 18 Ark. 338.

Of course there is no discharge if the change of location is authorized by the charter or contract of subscription. Danbury & Norwalk R. Co. v. Wilson, 22 Conn. 435; State v. Atchafalaya Railroad & Banking Co., 5 Rob. (La.) 63;

Williamsport & Hagerstown Turnpike Co. v. Hollman, 8 Gill & J. (Md.) 75; Ellison v. Mobile & Ohio R. Co., 36 Miss. 572; or if there is no condition in the subscription against a change of route, Colvin v. Liberty & Abington Turnpike Co., 2 Ind. 511; Lackey v. Richmond & Lancaster Turnpike Road Co., 17 B. Mon. (Ky.) 43; Smith v. Gower, 2 Duv. (Ky.) 17; Greenville & Columbia R. Co. v. Coleman, 5 Rich. Law (S. C.) 118; Greenville & P. R. Narrow Gauge R. Co. v. Johnson, 8 Baxt. (Tenn.) 332; or if the subscriber expressly or impliedly consents to the change, North Carolina R. Co. v. Leach, 4 Jones Law (N. C.) 340.

The deviation from the route fixed by the charter or contract of subscription must be a material deviation to operate as a discharge. Williamsport & Hagerstown Turnpike Co. v. Hollman, 8 Gill & J. (Md.) 75; Greenville & Columbia R. Co. v. Coleman, 5 Rich. Law (S. C.) 118.

Mere formal irregularity in relocation of the road does not discharge subscribers. Boston, Barre & G. R. Co. v. Wellington, 113 Mass. 79.

521 Freemont Ferry & Bridge Co. v. Fuhrman, 8 Neb. 99.

522 Auburn Bolt & Nut Works v. Shultz, 143 Pa. St. 256.

and that it has suspended operations, for there can be no breach of the guaranty before the subscription is paid.<sup>523</sup>

## § 482. Discharge by alteration or amendment of charter.

If a corporation, after subscriptions to its capital stock, procures or accepts an alteration or amendment of its charter, whereby its character, object, or powers are materially or fundamentally changed, there is a material alteration of the contracts of the subscribers, and it follows that those who do not assent to the change are discharged from liability on their subscriptions. And they may set up the alteration or amendment as a defense in an action to enforce their subscriptions, whether the action is brought by the corporation itself, or by creditors, or by a receiver or assignee in bankruptey.<sup>524</sup> As was said in substance

<sup>523</sup> Miller v. Pittsburgh & Connellsville R. Co., 40 Pa. St. 237, 80 Am. Dec. 570.

524 United States: Clearwater v. Meredith, 1 Wall. 25; Nugent v. Supervisors of Putnam County, 19 Wall. 241; Ashton v. Burbank, 2 Dill. 435, Fed. Cas. No. 582.

Arkansas: Witter v. Mississippi, Ouachita & R. R. R. Co., 20 Ark. 463.

Florida: Martin v. Pensacola & Georgia R. Co., 8 Fla. 370, 73 Am.

Georgia: Winter v. Muscogee R. Co., 11 Ga. 438; Academy of Music v. Flanders, 75 Ga. 14; Snook v. Georgia Improvement Co., 83 Ga. 61.

Illinois: Supervisors of Fulton County v. Mississippi & Wabash R. Co., 21 Ill. 338; Illinois Grand Trunk R. Co. v. Cook, 29 Ill. 237.

Indiana: Sparrow v. Evansville & Crawfordsville R. Co., 7 Ind. 369; Fisher v. Evansville & Crawfordsville R. Co., 7 Ind. 407; McCray v. Junction R. Co., 9 Ind. 358; Booe v. Junction R. Co., 10 Ind. 93; State v. Bailey, 16 Ind. 46, 79 Am. Dec. 405; Shelbyville & Rushville Turnpike Co. v. Barnes, 42 Ind. 498.

Maine: Oldtown & Lincoln R. Co. v. Veazie, 39 Me. 571. Massachusetts: Middlesex Turnpike Corp. v. Swan, 10 Mass. 384, 6 Am. Dec. 139; Middlesex Turnpike Corp. v. Locke, 8 Mass. 268.

Michigan: Tuttle v. Michigan Air Line R. Co., 35 Mich. 247.

Mississippi: Hester v. Memphis & Charleston R. Co., 32 Miss. 378; New Orleans, Jackson & G. N. R. Co. v. Harris, 27 Miss. 517; Champion v. Memphis & Charleston R. Co., 35 Miss. 692.

New Hampshire: Union Locks & Canals v. Towne, 1 N. H. 44, 8 Am. Dec. 32.

New York: Hartford & New Haven R. Co. v. Croswell, 5 Hill, 383, 40 Am. Dec. 354, 2 Keener's Cas. 1262, 1 Smith's Cas. 230, 1 Cum. Cas. 894; Troy & Rutland R. Co. v. Kerr, 17 Barb. 581.

North Carolina: First Nat. Bank v. City of Charlotte, 85 N. C. 433; Thompson v. Guion, 5 Jones Eq. 113.

Ohio: Marietta & Cincinnati R. Co. v. Elliott, 10 Ohio St. 57.

Co., 9 Ind. 358; Booe Pennsylvania: Manheim, P. & R. Co., 10 Ind. 93; L. Turnpike or Plank Road Co. v. iley, 16 Ind. 46, 79 Am. Arndt, 31 Pa. St. 317; Indiana & Shelbyville & Rushville Ebensburg Turnpike Road Co. v. Phillips, 2 Pen. & W. 184; Southern Pennsylvania Iron & R. Co. v. Oldtown & Lincoln R. Stevens, 87 Pa. St. 190.

Virginia: Norwich Lock Mfg.

in an early New Hampshire case: "Every individual owner of shares expects, and indeed stipulates, with the other owners, as a corporate body, to pay them his proportion of the expense, which a majority may please to incur, in the promotion of the particular object of the corporation. By acquiring an interest in the corporation, therefore, he enters into an obligation with it, in the nature of a special contract, the terms of which contract are limited by the specific provisions, rights and liabilities, detailed in the act of incorporation. To make a valid change in this private contract, as in any other, the assent of both parties is indispensable. The corporation, on one part, can assent by a vote of the majority; the individual, on the other part, by his own personal act. However the corporation, then, may be bound by the assent to the additional acts, a dissenting subscriber, in his individual capacity, having never consented thereto, is under no obligations to the corporation, except what he incurred by becoming a member under the first act."525 The mere fact that an amendatory act is clearly beneficial to the corporation and the stockholders, or that it is for a laudable object of public utility, cannot render it binding upon a dissenting stockholder, for he has a right to stand strictly upon the terms of his contract of membership. Notwithstanding the laudable object and great utility of the amendment, still, if it effects a material change, a dissenting stockholder, when sued upon his subscription, is able to say: "Non haec in federa veni." 526

According to the weight of authority, a subscriber is discharged by a material and fundamental alteration or amendment of the charter of the corporation, even when the legislature has the reserved power to alter, amend, or repeal the char-

Co. v. Hockaday, 89 Va. 557.

Wisconsin: Kenosha, Rockford 574. & R. I. R. Co. v. Marsh, 17 Wis. 13, & R. I. R. Co. v. Marsh, 17 Wis. 13, 525 Union Locks & Canals v. 2 Keener's Cas. 1266, 1 Cum. Cas. Towne, 1 N. H. 44, 8 Am. Dec. 32.

a promissory note given to the cor- Am. Dec. 32.

poration is not affected by altera-West Virginia: Greenbrier Industrial Exposition v. Rodes, 37 W. has ceased to be a stockholder. Va. 738. Mitchell v. Rome R. Co., 17 Ga.

526 Woodbury, J., in Union Locks

The liability of a subscriber on & Canals v. Towne, 1 N. H. 44, 8

ter, for such a reservation of power is not construed as authorizing the legislature or a majority of the stockholders to bind a dissenting stockholder by an amendment which is radical or fundamental, so as to make the corporation or the undertaking something essentially different from what was intended by the subscribers at the time of their subscriptions. 527

There is no discharge of dissenting subscribers, however, by an alteration or amendment of the charter of the corporation, under the reserved power to alter, amend, or repeal, or even where there is no such reserved power, where it does not fundamentally or materially change the character, objects, or powers of the corporation, but is merely in furtherance of the original purpose. 528 The question as to what alterations are material or fundamental will be considered at length in a

Co. v. Marsh, 17 Wis. 13, 2 Keener's Cas. 1266, 1 Cum. Cas. 897; Troy & Rutland R. Co. v. Kerr, 17 Barb. (N. Y.) 581; and many other cases in note 524, supra. And see post, chapter xxiv., § 631(f)(2).

<sup>528</sup> United States: Clearwater v. Meredith, 1 Wall. 25; Nugent v. Supervisors of Putnam County, 19 Wall. 241; Priest v. Glenn, 4 U. S. App. 478, 51 Fed. 400; Glenn v. Springs, 26 Fed. 494; Payson v. Withers, 5 Biss. 269, Fed. Cas. No. 10,864; Payson v. Stoever, 2 Dill. 427, Fed. Cas. No. 10,863.

Arkansas: Jacks v. City of Helena, 41 Ark. 213; Witter v. Mississippi, Ouachita & R. R. R. Co., 20

Delaware R. Co. v. Delaware: Tharp, 1 Houst. 149.

Georgia: Wilson v. Wills Valley R. Co., 33 Ga. 466; Howard v. Glenn, 85 Ga. 238, 21 Am. St. Rep. 156; Chattanooga, Rome & C. R. Co. v. Warthen, 98 Ga. 599.

Banet v. Alton & San-Illinois: gamon R. Co., 13 Ill. 504; Sprague v. Illinois River R. Co., 19 Ill. 174; Rice v. Rock Island & Alton R.

527 Kenosha, Rockford & R. I. R. Earp, 21 III. 291; Corwith v. Culver, 69 III. 502.

> Indiana: Hanna v. Cincinnati & Ft. Wayne R. Co., 20 Ind. 30; Hayworth v. Junction R. Co., 13 Ind.

> Iowa: Peoria & Rock Island R. Co. v. Preston, 35 Iowa, 115.

> Kentucky: Glover v. Myer, 3 Ky.

Law Rep. 181. Maine: South Bay Meadow Dam Co. v. Gray, 30 Me. 547; Bucksport & Bangor R. Co. v. Buck, 68 Me.

Maryland: Taggart v. Western Maryland R. Co., 24 Md. 563, 89 Am. Dec. 760.

Massachusetts: Agricultural Branch R. Co. v. Winchester, 13 Al-

Missouri: Pacific R. Co. v. Hughes, 22 Mo. 291, 64 Am. Dec. 265; Pacific R. Co. v. Renshaw, 18 Mo. 210.

New Jersey: Delaware & Atlantic R. Co. v. Irick, 23 N. J. Law,

New York: Buffalo & New York City R. Co. v. Dudley, 14 N. Y. 336, 2 Smith's Cas. 742; Schenectady & Saratoga Plank Road Co. v. Co., 21 III. 93; Illinois River R. Thatcher, 11 N. Y. 102; Troy & Rut-Co. v. Beers, 27 Ill. 185; Peoria & land R. Co. v. Kerr, 17 Barb. 581; Oquawka R. Co. v. Elting, 17 Ill. Union Hotel Co. v. Hersee, 79 N. 429: Terre Haute & Alton R. Co. v. Y. 454: Poughkeepsie & Salt Point

subsequent chapter, in treating generally of the power of the majority of the stockholders to bind the minority, for as to this question there is no difference between cases in which the alteration is set up as a defense in an action against a dissenting stockholder on his subscription and cases in which a dissenting stockholder sues to enjoin the corporation from accepting or making the alteration. 529

Nor is there any discharge of a subscriber by reason of an alteration or amendment which is authorized by the charter of the corporation or by a general law in force at the time of his subscription, for in such a case the right of a majority to bind him by the amendment is a term of his contract. 530

Nor are subscribers discharged where they consent to the alteration or amendment at the time it is made, or afterwards. And if a subscriber with knowledge fails to give notice of his dissent within a reasonable time, it is equivalent to consent. 531

454, 24 N. Y. 150.

Ohio: Pennsylvania & Ohio Canal Co. v. Webb, 9 Ohio, 136; Jewett v. Valley Ry. Co., 34 Ohio St. 601; Armstrong v. Karshner, 47 Ohio St. 276; Milford & Chillicothe Turnpike Co. v. Brush, 10 Ohio, 111, 36 Am. Dec. 78.

Pennsylvania: Clark v. Monongahela Navigation Co., 10 Watts, 364; Irvin v. Susquehanna & Phillipsburg Turnpike Co., 2 Pen. & W. 466, 23 Am. Dec. 53; Gray v. Monongahela Navigation Co., 2 Watts & S. 156, 37 Am. Dec. 500; Cross v. Peach Bottom Ry. Co., 90 Pa. St. 392; Com. v. City of Pittsburgh, 41 Pa. St. 278.

South Carolina: Greenville Columbia R. Co. v. Coleman, Rich. Law, 118.

Vermont: Connecticut & Passumpsic Rivers R. Co. v. Bailey, 24 Vt. 465, 58 Am. Dec. 181; Rutland & Burlington R. Co. v. Thrall, 35 Vt. 536.

529 See post, chapter xxiv.

Plank Road Co. v. Griffin, 21 Barb. Sparrow v. Evansville & Crawfordsville R. Co., 7 Ind. 369; Bish v. Johnson, 21 Ind. 299; Witter v. Mississippi, Ouachita & R. R. R. Co., 20 Ark. 463; Mansfield, Coldwater & L. M. R. Co. v. Brown, 26 Ohio St. 223; Mansfield, Coldwater & L. M. R. Co. v. Stout, 26 Ohio St. 241; Jewett v. Valley Ry. Co., 34 Ohio St. 601; Fry v. Lexington & Big Sandy R. Co., 2 Metc. (Ky.) 314.

531 Martin v. Pensacola & Georgia R. Co., 8 Fla. 370, 73 Am. Dec. 713; Marietta & Cincinnati R. Co. v. Elliott, 10 Ohio St. 57; Bedford R. Co. v. Bowser, 48 Pa. St. 29.

Dissent and notice thereof must be shown by the subscriber in an action on his subscription. It is not incumbent upon the corporation to show his assent. Martin v. Pensacola & Georgia R. Co., 8 Fla. 370, 73 Am. Dec. 713.

In Massachusetts, where it is held, as we shall see, that no promise to pay assessments is to be implied from the mere fact of a sub-530 Nugent v. Supervisors of Put- scription to shares in a corporanam County, 19 Wall. (U. S.) 241; tion, the charter of which gives Edwards v. People, 88 III. 340; the corporation a special remedy

There is no discharge in any case unless the alteration or amendment is actually made. The mere passage of an act amending the charter of a corporation by conferring additional powers, or authorizing an amendment, does not release subscribers, where the corporation does not accept the same, or does not attempt or is not permitted to take advantage of it.532

### § 483. Discharge by formation of a different corporation from that contemplated.

Where a person subscribes for stock in a corporation to be subsequently formed, and a corporation of a different character from that contemplated, or with different powers, is formed, without his consent to the change, he is not liable on his subscription. This, however, is not a case of release or discharge from liability, for there has never been any contract at all.533

# Discharge by consolidation.

A subscriber for stock in a corporation is discharged from any liability on his subscription if the corporation is consoli-

of assessments, and that an express promise, therefore, is necessary to sustain an action of assumpsit to recover assessments, it has been held that consent of a subscriber for shares in a corporation to an alteration by the legislature of its object will not render him liable to the corporation on an express promise to pay assessments made before the alteration, and his consent thereto, but that the only remedy of the corporation is to sell his shares. Middlesex Turnpike Corp. v. Swan, 10 Mass. 384, 6 Am. Dec. 139. The court, however, might very well have held in this case that, in consenting to the alteration of the road, the subscriber impliedly, not as a matter of law merely, but as a matter of fact (for such would seem clearly to have been the intention), consented to a correspond- cases there cited.

by sale of shares for nonpayment ing alteration of his express promise to pay assessments.

> 532 Fry v. Lexington & Big Sandy R. Co., 2 Metc. (Ky.) 314; State v. Atchafalaya Railroad & Banking Co., 5 Rob. (La.) 63; Hawkins v. Mississippi & Tennessee R. Co., 35 Miss. 688; Rutland & Burlington R. Co. v. Thrall, 35 Vt. 536; Chattanooga, Rome & C. R. Co. v. Warthen, 98 Ga. 599; Mississippi, Ouachita & R. R. Co. v. Gaster, 24 Ark. 96.

> In a Mississippi case it was held that a subscriber for stock in a railroad company was not discharged by its acceptance of an amendment authorizing it to build a branch, where it had not proposed to build it. Hawkins v. Mississippi & Tennessee R. Co., 35 Miss. 688.

> 533 See ante, § 439(d), and the

dated with another under a statute passed after the subscription, where the state has not reserved the power to alter, amend, or repeal the charter, if he does not consent to the consolidation.<sup>534</sup> And by the weight of authority he is discharged, even though the power to alter, amend, or repeal the charter has been reserved, if the consolidated corporation is radically different from the original corporation in its nature, constitution, or powers.535

There is no discharge, however, where the power to alter, amend, or repeal the charter has been reserved, and the consolidation does not make a radically different corporation, but merely carries out the objects originally intended. 536 there any discharge from liability if the consolidation is authorized by the charter of the corporation, or by a general law in force at the time the subscription was made;537 or if he consents to the consolidation, and it has been held that failure to give notice of dissent within a reasonable time is equivalent to consent.538

#### § 485. Special agreements with, or release of, or nonpayment by, other stockholders.

A subscriber, when sued upon his subscription, cannot set up as a defense that the corporation has made special agreements with other stockholders, or has released other stockholders, unless his subscription is voidable for fraud in its pro-

534 Tuttle v. Michigan Air Line Turnpike Co. v. Barnes, 42 Ind. R. Co., 35 Mich. 247; Supervisors of Fulton County v. Mississippi & Wabash R. Co., 21 Ill. 338; Illinois Grand Trunk R. Co. v. Cook, 29 Ill. Sparrow v. Evansville & Crawfordsville R. Co., 7 Ind. 369; v. Junction R. Co., 10 Ind. 93; State Brown, 26 Ohio St. 223; Mansfield, v. Bailey, 16 Ind. 46, 79 Am. Dec. Coldwater & L. M. R. Co. v. Stout, 405; Shelbyville & Rushville Turn- 26 Ohio St. 241. pike Co. v. Barnes, 42 Ind. 498.

536 Hanna v. Cincinnati & Ft. Wayne R. Co., 20 Ind. 30.

537 Edwards v. People, 88 Ill. 340; Sprague v. Illinois River R. Co., 19 III. 177; Sparrow v. Evansville Fisher v. Evansville & Crawfords- & Crawfordsville R. Co., 7 Ind. 369; ville R. Co., 7 Ind. 407; McCray v. Bish v. Johnson, 21 Ind. 299; Mans-Junction R. Co., 9 Ind. 358; Booe field, Coldwater & L. M. R. Co. v.

538 Martin v. Pensacola & Geor-535 Booe v. Junction R. Co., 10 gia R. Co., 8 Fla. 370, 73 Am. Dec. Ind. 93; Shelbyville & Rushville 713.

curement,539 for if the special agreement or release is in fraud of his rights, it is void as against him, and if it is valid he has no ground for complaint.540

A subscriber is not discharged by failure of other subscribers to pay their subscriptions.541

### § 486. No discharge by exercise of powers granted by charter or general law.

It is clear that a subscriber is not discharged from liability on his subscription by the exercise by the corporation of any power which is conferred upon it, either expressly or impliedly, by its charter, or by a general law in force at the time of the subscription, for the provisions of the charter or law enter into and form a part of the contract of subscription. Every subscriber for stock in a corporation contracts with reference to the powers conferred upon the corporation at the time of the subscription.542 It has been held, therefore, that

### 539 Ante, § 468 et seq.

540 Dorman v. Jacksonville & Alligator Plank-Road Co., 7 Fla. 265; Macon & Augusta R. Co. v. Vason, 57 Ga. 314; Whittlesey v. Frantz, 74 N. Y. 456; Nickerson v. English, 142 Mass. 267; Connecticut & Pasnonperformance of the condition. Sumpsic Rivers R. Co. v. Bailey, See post, § 505. And see Memphis 24 Vt. 465, 60 Am. Dec. 283; In re Branch R. Co. v. Sullivan, 57 Ga. Republic Ins. Co., 3 Biss. 452, Fed. 240; New York Exchange Co. v. Cas. No. 11,704; Swatara R. Co. v. De Wolf, 31 N. Y. 273.

McKim, Fed. Cas. No. 13,681; Howard v. Glenn, 85 Ga. 238, 21 Am. Vason, 57 Ga. 314; Cook v. Hopst. Rep. 156; Galena & Southern kinsville, N. & B. Turnpike Road Wisconsin R. Co. v. Ennor, 116 Ill. Co. (Ky.) 32 S. W. 748; Little v. 55; Jewell v. Rock River Paper Obrien, 9 Mass. 423; Hamilton v. Co. 101 Ill. 57; Fey v. Peoria Tarlton, 3 Ky Law Rep. 471. Co., 101 III. 57; Fey v. Peoria Watch Co., 32 III. App. 618; Western Plank-Road Co. v. Stockton, 7 Ind. 500; Anderson v. Newcastle & Richmond R. Co., 12 Ind. 376, 74 Am. Dec. 218; Armstrong v. Danahy, 75 Hun, 405, 27 N. Y. Supp. 60; ford v. Pittsburgh & Erie R. Co., ter v. Dickinson, 6 Gray (Mass.) 32 Pa. St. 141; Jewett v. Valley Ry. 586; Gibbons v. Grinsel, 79 Wis. Co., 34 Ohio St. 601; Wilson v. 365.

Hundley, 96 Va. 96. And see ante, §§ 467, 476.

Of course this does not apply so as to prevent a subscriber, whose subscription is upon condition that a certain amount of stock shall be subscribed or paid, from showing nonperformance of the condition.

Tarlton, 3 Ky. Law Rep. 471.

542 Ottawa, Oswego & F. R. V. R. Co. v. Black, 79 Ill. 262; Armstrong v. Karshner, 47 Ohio St. 276; Port Edwards, Centralia & N. Ry. Co. v. Arpin, 80 Wis. 214; White v. Butler University, 78 Ind. Bristol Iron & Steel Co. v. Selliez, 585; Ginrich v. Patrons' Mill Co., 175 Pa. St. 18; County of Craw- 21 Kan. 61; City Hotel in Worcesa subscriber for stock in a railroad company is not discharged from liability by the fact that the company has leased its road, 543 or sold the whole or a part of its road, 544 or increased its capital stock, etc., 545 in pursuance of a power conferred upon it prior to the subscription.

# Mismanagement of the corporation-Illegal election of officers, etc.

If the affairs of a corporation are mismanaged by the directors or other officers, or by the majority of the stockholders, stockholders not participating in the fraudulent or wrongful acts or neglect have a remedy in equity by suit for an injunction, or to hold the guilty officers or stockholders liable to the corporation for any damages sustained by the corporation; but mismanagement of a corporation does not discharge a stockholder from liability on his subscription, and is no defense in an action thereon.546

Irregularity or illegality in the election of the directors of a corporation, or other officers, or disqualification, while it may be ground for quo warranto proceedings to oust them, does not discharge subscribers, or constitute any defense in actions on subscriptions.547

The same is true of irregularities in adopting by-laws 548 or the adoption of an illegal by-law restricting the right of subscribers to vote.549

543 Ottawa, Oswego & F. R. V. R. 422; Co. v. Black, 79 Ill. 262.

544 Armstrong v. Karshner, 47 Ohio St. 276.

545 Port Edwards, Centralia & N.Ry. Co. v. Arpin, 80 Wis. 214.

546 Hards v. Platte Valley Improvement Co., 46 Neb. 709; American Building & Loan Ass'n v. Rainbolt, 48 Neb. 434; Merrill v. Reaver, 50 Iowa, 404; Goff v. Hawkeye

422; People v. Logan County Sup'rs, 63 Ill. 374; Chetlain v. Re-public Life Ins. Co., 86 Ill. 220; Courtright v. Deeds, 37 Iowa, 503; Hannibal, R. C. & P. Plank-Road Co. v. Menefee, 25 Mo. 547; Chouteau Ins. Co. v. Floyd, 74 Mo. 286; Glenn v. Rosborough, 48 S. C. 272; Cook v. Hopkinsville, N. & B. Turnpike Road Co. (Ky.) 32 S. W. 748; Oldham v. Mt. Sterling Improvement Co. (Ky.) 45 S. W. 779; Pump & Windmill Co., 62 Iowa, provement Co. (Ky.) 45 S. W. 779; 691; Smith v. Tallassee Branch of First Municipality of City of New Central Plank-Road Co., 30 Ala. Orleans v. Orleans Theatre Co., 2 650; Hornaday v. Indiana & Illi-Rob. (La.) 209; Southern Life Innois Central Ry. Co., 9 Ind. 263; surance & Trust Co. v. Lanier, 5 People v. Town of Barnett, 91 III. Fla. 110, 58 Am. Dec. 448; Cravens

### § 488. Failure to comply with provisions of charter or general law-Ultra vires acts.

As we have seen, there is no liability upon subscriptions for stock in a corporation to be formed, in the absence of an estoppel, unless the corporation is legally formed as contemplated. And therefore a failure to comply with conditions precedent to incorporation prescribed by the legislature may be set up as a defense in an action on a preliminary subscription. 550 very different, however, where a corporation has acquired a legal existence, and has since failed to comply with conditions subsequent,551 or where it has engaged in acts constituting a misuser or abuse of its powers. While the state may institute proceedings to forfeit the charter of a corporation for failure to comply with conditions subsequent prescribed therein or in the general law, or for nonuser of its franchises, or for misuser or abuse thereof by engaging in ultra vires acts, and while a stockholder may sue to enjoin ultra vires acts, it is well settled that neither noncompliance by a corporation with conditions subsequent in its charter or the general law, nor ultra vires acts, can be relied upon by a stockholder as a discharge from liability on his subscription,552 unless by express legislative pro-

v. Eagle Cotton Mills Co., 120 Ind. 6, 16 Am. St. Rep. 298; Urner v. Sollenberger, 89 Md. 316. See, also,

Hills, 6 Cow. (N. Y.) 23, 16 Am. Dec. 429; Steinmetz v. Versailles & Osgood Turnpike Co., 57 Ind. 457; Covington, C. C. & J. Plank Road Co. v. Moore, 3 Ind. 510; Johnson v. Crawfordsville, F. K. & Ft. W. R. Co., 11 Ind. 280; Eakright v. Logansport & Northern Indiana R. Co., 13 Ind. 404; Ginrich v. Patrons' Mill Co., 21 Kan. 61; Central Plank Road Co. v. Clemons, 16 Mo. 359; Ross v. Bank of Gold Hill, 20 Nev. 191.

R. Co., 18 III. 190.

550 Ante, §§ 439(c), 462(e).

551 Ante, § 73. 552 Naugatuck Water Co. v. Nichols, 58 Conn. 403; Troy & Rutland 547 Trustees of Vernon Society v. R. Co. v. Kerr, 17 Barb. (N. Y.) 581; Connecticut & Passumpsic Rivers R. Co. v. Bailey, 24 Vt. 465, 58 Am. Dec. 181; Taggart v. Western Maryland R. Co., 24 Md. 563, 89 Am. Dec. 760; Musgrave v. Morrison, 54 Md. 161; Cravens v. Eagle Cotton Mills Co., 120 Ind. 6, 16 Am. St. Rep. 298; Penobscot R. Co. v. White, 41 Me. 512, 66 Am. Dec. 257; Cartwright v. Dickinson, 88 Tenn. 476, 17 Am. St. Rep. 910: Voorhees v. Bank of Circleville, 19 Ohio, 463; McDermott v. Donegan, 548 Ginrich v. Patrons' Mills Co., 44 Mo. 85; Toledo & Ann Arbor R. Co. v. Johnson, 49 Mich. 148: Unit-549 Chandler v. Northern Cross ed States Vinegar Co. v. Schlegel, 143 N. Y. 537; United States Vine-

vision such noncompliance or abuse on the part of the corporation ipso facto terminates its corporate existence, so that there is no longer any corporation to enforce the subscription.<sup>553</sup> If for such a cause the charter of the corporation is subject to forfeiture, it is exclusively a question between the state and the corporation, and if the state sees fit to waive the forfeiture, no one else can take advantage of it.554

Thus, a subscriber is not discharged from liability by failure of a corporation to comply with a statutory provision that its capital stock shall be paid within two years after incorporation, and that, for breach of such condition, it shall be dissolved;555 or by failure of a railroad company to comply with a charter requirement that it shall expend a certain amount in the construction of its road within a certain time, or forfeit its charter; 556 or that it shall commence the construction of its road within a certain time;557 or by failure of a corporation to

gar Co. v. Foehrenbach, 148 N. Y. Northern Ry. Co., 73 Tex. 624, 58; Russell v. Alabama Midland And see ante, § 306. Ry. Co., 94 Ga. 510; Mississippi, Even in such a case, a court of Ouachita & R. R. Co. v. Cross, equity could enforce payment of Life Ins. Co., 86 Ill. 220; Fey v. Peoria Watch Co., 32 Ill. App. 618; Hannibal, R. C. & P. Plank Road exist by reason of noncompliance Co. v. Menefee, 25 Mo. 547; Smith with a condition subsequent, so Plank-Road Co., 30 Ala. 650; Merrill v. Reaver, 50 Iowa, 404; Goff and rendered binding by an act of v. Hawkeye Pump & Windmill Co., the legislature without the sub-62 Iowa, 691; Hornaday v. In-scribers' consent. Greencastle & diana & Illinois Central Ry. Co., 9 M. L. Turnpike & Plank Road Co. Ind. 263; People v. Logan County v. Davidson, 39 Pa. St. 435. Sup'rs, 63 Ill. 374; First Munici-Sup'rs, 63 Ill. 374; First Municipality of City of New Orleans v. Rivers R. Co. v. Bailey, 24 Vt. 465, Orleans Theatre Co., 2 Rob. (La.) 58 Am. Dec. 181; Taggart v. West-209; Central Plank Road Co. v. ern Maryland R. Co., 24 Md. 563, Orleans Theatre Co., 2 Rob. (La.) 209; Central Plank Road Co. v. Clemens, 16 Mo. 359; Hanover Junction & Susquehanna R. Co. v. Haldeman, 82 Pa. St. 36.

553 McCully v. Pittsburgh & Con-nellsville R. Co., 32 Pa. St. 25; Greencastle & M. L. Turnpike & Rivers R. Co. v. Bailey, 24 Vt. 465, Plank Road Co. v. Davidson, 39 Pa. 58 Am. Dec. 181. St. 435; Sodus Bay & Corning R. 557 Taggart v. Western Mary-Co. v. Lapham, 43 Hun (N. Y.) land R. Co., 24 Md. 563, 89 Am. 314; Bywaters v. Paris & Great Dec. 760.

20 Ark. 443; Chetlain v. Republic subscriptions for the benefit of creditors. See ante, § 326.

Where a charter has become void Courtright v. Deeds, 37 Iowa, 503; and the corporation has ceased to Tallassee Branch of Central that subscriptions are discharged; they cannot be aferwards revived

89 Am. Dec. 760; and other cases in note 552, supra. See ante, § 313.

555 Musgrave v. Morrison, 54 Md.

file a certificate of organization; 558 or by the fact that the corporation has violated a prohibition in its charter against entering into a contract or engaging in other business before subscription or payment, or both, of the whole or a certain percentage of its capital stock; 559 or by the fact that it has made an ultra vires lease or conveyance of its property;560 or illegally attempted to increase its capital stock since the subscription, the increase being void;561 or illegally issued bonds;562 or purchased stock in another corporation, and an expensive building, beyond its means;563 or engaged in an illegal business by joining a trust, or otherwise. 564

# Nonuser or abandonment of enterprise on the part of the corporation.

Upon the principle stated in the preceding section, mere nonuser of its franchises by a corporation, although it may be such as to render its charter liable to forfeiture in proceedings by

v. Gade, 55 Ill. App. 181.

Co. 559 Naugatuck Water Nichols, 58 Conn. 403; Agricultural Branch R. Co. v. Winchester, 13 Allen (Mass.) 29; Branch v. Augusta Glass Works, 95 Ga. 573; McDermott v. Donegan, 44 Mo. 85.

A charter or statutory requirement that a certain percentage of the cost shall be subscribed before a railroad company shall commence the construction of any section of its road does not affect the organization of the company, and noncompliance therewith is no defense in an action to collect assessments on subscriptions. Penobscot R. Co. v. White, 41 Me. 512, 66 Am. Dec. 257.

Bonds given in payment for the capital stock of an insurance company, on which the company issued certificates of stock and engaged in not be relieved business, will against in equity because the capital stock was not in good faith Schlegel, 143 N. Y. 537; United paid in, and the company violated the express provisions of its charter in embarking in business. Midland Ry. Co., 94 Ga. 510.

558 Forest Glen Brick & Tile Co. Yard v. Pacific Mutual Ins., Co., 10

Yard v. Pacine Mutual Ins., Co., 10 N. J. Eq. 480, 64 Am. Dec. 467. 560 Troy & Rutland R. Co. v. Kerr, 17 Barb. (N. Y.) 581; Illi-nois Midland Ry. Co. v. Town of Barnett, 85 Ill. 313; Hays v. Ot-tawa, Oswego & F. R. V. R. Co., 61 Ill. 422.

Contra, South Georgia & Florida R. Co. v. Ayres, 56 Ga. 230.

Subscribers for stock in a railroad company are not discharged by a sale of all its property to another company, where the sale is rescinded. Chattanooga, Rome & C. R. Co. v. Warthen, 98 Ga. 599.

561 Cartwright v. Dickinson, 88 Tenn. 476, 17 Am. St. Rep. 910. And see ante, § 407(g).

Compare Merrill v. Gamble, 46 Iowa, 615.

562 Merrill v. Reaver, 50 Iowa,

563 Chetlain v. Republic Life Ins. Co., 86 Ill. 220.

the state, cannot be set up by a subscriber as a discharge from liability on his subscription. There cannot be a shadow of doubt as to the soundness of this proposition where there are creditors to be paid. And it is equally well settled that it applies as between the subscriber and the corporation.565 is a subscriber discharged by delay on the part of the corporation in constructing its works or otherwise carrying out its objects, where there has been no abandonment of the enterprise; 566 or by the fact that the corporation has temporarily abandoned the enterprise, 567 or permanently abandoned a part of it. 568 Sale of a railroad on foreclosure of a mortgage thereon does not discharge subscribers.569

Even a permanent abandonment or failure of the enterprise will not discharge a subscriber where payment of his subscription is necessary for the satisfaction of debts of the corporation, or for adjustment as between the stockholders.<sup>570</sup> But a permanent abandonment or total failure will operate as a dis-

R. Co. v. Cross, 20 Ark. 443; Hammett v. Little Rock & Napoleon R. Co., 20 Ark. 204; McMillan v. Maysville & Lexington R. Co., 15 B. Mon. (Ky.) 218, 61 Am. Dec. 181; Anderson v. Middle & East Tennessee Central R. Co., 91 Tenn. 44: Gibson v. Columbia & New Richmond Turnpike & Bridge Co., 18 Ohio St. 396.

A subscriber is not discharged from liability by the fact that the corporation is in the hands of a receiver, for the receiver has the power to issue stock on payment of subscriptions, and the fact of receivership, therefore, is no defense in an action on a subscription by an assignee thereof. Chattanooga, Rome & C. R. Co. v. Warthen, 98 Ga. 599.

566 McMillan v. Maysville & Lexington R. Co., 15 B. Mon. (Ky.) 218, 61 Am. Dec. 181; Gibson v. Columbia & New Richmond Turn-

565 Mississippi, Ouachita & R. R. ford, 29 Iowa, 579; Pickering v. Templeton, 2 Mo. App. 424.

567 McMillan v. Maysville & Lexington R. Co., 15 B, Mon. (Ky.) 218, 61 Am. Dec. 181.

A temporary injunction against proceeding with its works is no de-

proceeding with its works is no defense in an action on a subscription. Crossman v. Penrose Ferry Bridge Co., 26 Pa. St. 69.

568 Buffalo & Jamestown R. Co. v. Gifford, 87 N. Y. 294; Dallas Cotton & Woolen Mills v. Clancey (Tex.) 15 S. W. 194; Dorman v. Jacksonville & Alligator Plank-Road Co., 7 Fla. 265; Vicksburg, Shreveport & T. R. Co. v. McKean, 12 La. Ann 638 See also Arm-12 La. Ann. 638. See, also, Armstrong v. Karshner, 47 Ohio St. 276.

569 Buffalo & Jamestown R. Co. v. Gifford, 87 N. Y. 294.

570 Hardy v. Merriweather, 14 Ind. 203; Bish v. Bradford, 17 Ind. 490: McMillan v. Maysville & Lexington R. Co., 15 B. Mon. (Ky.) 218, 61 Am. Dec. 181; Phoenix pike & Bridge Co., 18 Ohio St. 396; Warehousing Co. v. Badger, 67 N. Miller v. Pittsburgh & Connells- Y. 294; Four Mile Valley R. Co. v. ville R. Co., 40 Pa. St. 237, 80 Am. Bailey, 18 Ohio St. 208; Chouteau Dec. 570; First Nat. Bank v. Hur- Ins. Co. v. Floyd, 74 Mo. 286; Troy

charge as between the subscriber and the corporation, where there are no debts, nor any question as to the rights of the different stockholders.571

#### § 490. Delay in making calls, and the statute of limitations.

Lapse of time without making calls upon subscriptions does not operate to discharge a subscriber from liability on his subscription,572 unless it is sufficient to show an abandonment of the enterprise. 573 or to bring the case within the statute of limitations, 574 for "lapse of time, not amounting to the bar of limitations, is not a defense to an action at law."575

Statute of limitations.—In the absence of a special charter or statutory provision, an action on a subscription for stock, not under seal, is within the statute limiting the time for commencing actions upon contracts express or implied. The statute necessarily commences to run, in the absence of special circumstances, as soon as the right to maintain an action accrues,

(N. Y.) 581; Dill v. Wabash Valley R. Co., 21 Ill. 91.

Subscribers for stock in a railroad company are not released them and the corporation. from liability by the facts that the company has suspended operations upon the road, and that it will require a large additional expenditure of labor and money to com-plete its construction, or even by the fact that the means of the company are wholly inadequate to accomplish its object. McMillan v. Maysville & Lexington R. Co., 15 B. Mon. (Ky.) 218, 61 Am. Dec. 181; Anderson v. Middle & East Tennessee Central R. Co., 91 Tenn.

571 McMillan v. Maysville & Lexington R. Co., 15 B. Mon. (Ky.) 218, 61 Am. Dec. 181; Pittsburgh & Connellsville R. Co. v. Byers, 32 Pa. St. 22, 72 Am. Dec. 770; Delaware River & Lancaster R. Co. v. Rowland (Pa.) 9 Atl. 929; Blake v. Brown, 80 Iowa, 277.

If the corporation delays for a

& Rutland R. Co. v. Kerr, 17 Barb. ces as to lead subscribers to believe that it has abandoned the work, and they act upon such belief, they are discharged as between Jewell, 8 B. Mon. (Ky.) 140; Mc-Cully v. Pittsburgh & Connells-ville R. Co., 32 Pa. St. 25; Pittsburgh & Connellsville R. Co. v. Byers, 32 Pa. St. 22, 72 Am. Dec. 770; United States Wind-Engine & Pump Co. v. Davis, 2 Kan. App.

Subscribers are discharged by abandonment of the object of the corporation and reorganization without their consent. Bank of China, Japan & The Straits v. Morse, 44 App. Div. (N. Y.) 435.

572 Taggart v. Western Maryland R. Co., 24 Md. 563, 89 Am. Dec. Compare, however, Carter, Rittenberg & Hainlin Co. v. Hazzard, 65 Minn. 432.

573 Ante, § 489.

574 See infra, this section.

575 Taggart v. Western Maryland long time under such circumstan- R. Co., 24 Md. 563, 89 Am. Dec. 760. and not before. If a subscription is payable immediately, without any necessity for a call, or if it is payable on a day certain, the statute begins to run at once, or from the day when it becomes payable, as the case may be.576

In some of the cases it has been held that, even when a subscription is payable on demand or call by the directors, the statute begins to run from the date of the subscription, or, at the least, from a reasonable time after the subscription within which to call for payment.<sup>577</sup> If this rule, however, is really established in any jurisdiction, as it seems to be, it is contrary to decided weight of authority. When a subscription is only payable upon a call or assessment by the directors of the corporation, a call or assessment is necessary before the corporation can maintain any action against the subscriber. 578 And it is therefore held in most jurisdictions that, in such a case, the statute of limitations does not commence to run until a valid call or assessment is made, and it then runs against that call or assessment only.579

As in the case of other debts, the statute does not run while the

371; Hamilton v. Clarion, Mahoning & P. R. Co., 144 Pa. St. 34.

<sup>577</sup> See Pittsburgh & Connells-ville R. Co. v. Byers, 32 Pa. St. 22, 72 Am. Dec. 770; McCully v. Pittsburgh & Connellsville R. Co., 32 Pa. St. 26; Shackamaxon Bank v. Dougherty, 20 Wkly. Notes Cas. (Pa.) 297; Hamilton v. Clarion, Mahoning & P. R. Co., 144 Pa. St. 34; Great Western Telegraph Co. v. Purdy, 83 Iowa, 430; Id., 162 U. S. 329.

578 Post, § 498.

576 Curry v. Woodward, 53 Ala. con, 32 Fed. 7; Glenn v. Semple, 80 Ala. 159, 60 Am. Rep. 92; Lehman v. Glenn, 87 Ala. 618; Semple v. Glenn, 91 Ala. 245, 24 Am. St. Rep. 894; Western R. Co. v. Avery, 64 N. C. 491; Glenn v. Howard, 81 Ga. 383, 12 Am. St. 318; Lewis v. Glenn, 84 Va. 947; Vanderwerken v. Glenn, 85 Va. 9; In re Haggert Bros. Mfg. Co., 19 App. R. Ont. (Can.) 582.

A note given to a corporation in payment of stock is not a demand note where it is "payable in such installments and at such time or times as the directors may re-579 Taggart v. Western Maryland quire, notice thereof being pub-R. Co., 24 Md. 563, 89 Am. Rep. lished agreeably to the charter," 760; Glenn v. Williams, 60 Md. 93; which requires thirty days' publi-760; Glenn v. Williams, 60 Md. 93; which requires thirty days' publi-New England Fire Ins. Co. v. cation in a newspaper, and the Haynes, 71 Vt. 306, 76 Am. St. Rep. statute of limitations against an ac-771; Great Western Telegraph Co. tion thereon does not begin to run v. Gray, 122 Ill. 630; Hawkins v. from its date. New England Fire Glenn, 131 U. S. 319; Glenn v. Mar-Ins. Co. v. Havnes, 71 Vt. 306, 76 bury, 145 U. S. 499; Glenn v. Mar-Am. St. Rep. 771. subscriber resides out of the state, so that no action can be maintained against him.<sup>580</sup>

The effect of the statute of limitations as against the right of creditors, or of a receiver or assignee, to enforce payment of subscriptions, will be considered in a subsequent chapter.<sup>581</sup>

### VI. REMEDIES OF CORPORATION AGAINST SUBSCRIBERS.

§ 491. In general.—A corporation may, in all jurisdictions, maintain an action of assumpsit to recover the amount due on a subscription, or an installment due, if there is an express promise to pay; and in most jurisdictions it may maintain such an action without an express promise, a promise to pay being implied. The corporation is not precluded from maintaining such an action by the fact that the charter, articles of association, or general law gives it a remedy by forfeiture or sale of shares for nonpayment of assessments, unless this remedy is made exclusive, or has been pursued.

A corporation has no power to forfeit or sell the shares of a delinquent stockholder for nonpayment of assessments, unless the power is expressly conferred upon it by the charter, articles of association, or general law, or by consent of the stockholder; but such power is frequently conferred. In exercising this power, the provisions of the charter, articles of association, or general law, as to the mode of forfeiture or sale, notice, etc., must be strictly complied with.

# § 492. Action on subscriptions.

In all jurisdictions, a corporation may maintain an action of assumpsit to recover the amount of an unpaid and due subscription, or of an assessment or call thereon, if there is an express promise to pay the same, either in the subscription paper itself, or in a promissory note given by the subscriber, or otherwise. 582

In Massachusetts and several other states it has been held that, to sustain an action on a subscription for stock (at least

580 Tama Water-Power Co. v. 581 Post, chapter xxv. Hopkins, 79 Iowa, 653. 582 Worcester Turnpike Corp. v. when a remedy by forfeiture is given by statute),583 there must be an express promise to pay, and that no promise will be implied, the only remedy in the case of nonpayment, in the absence of an express promise, being by forfeiture or sale of the delinquent subscriber's shares.<sup>584</sup> In most states, however, the courts have taken a different view of a contract of subscription, and one which is more in consonance with the manifest intention of the parties, and have held that the mere fact of a subscription for shares of stock, and its acceptance by the corporation, raise an implied promise on the part of the subscriber to pay all valid assessments, upon which the corporation may maintain an action of assumpsit. 585 By the subscrip-

Willard, 5 Mass. 80, 4 Am. Dec. 39: Taunton & South Boston Turnpike Corp. v. Whiting, 10 Mass. 327, 6 Am. Dec. 124; Goshen & Minisink Turnpike Road v. Hurtin, 9 Johns. (N. Y.) 217, 6 Am. Dec. 273; Dutchess Cotton Manufactory v. Davis, 14 Johns. (N. Y.) 238, 7 Am. Dec. 459; Connecticut & Passumpsic Rivers R. Co. v. Bailey, 24 Vt. 465, 58 Am. Dec. 181.

583 Post, § 493. 584 Andover & Medford Turnpike Corp. v. Gould, 6 Mass. 40, 4 Am. Dec. 80; New Bedford & Bridgewater Turnpike Corp. v. Adams, 8 Mass. 138, 5 Am. Dec. 81; Middlesex Turnpike Corp. v. Swan, 10 Mass. 384, 6 Am. Dec. 139; Mechanics' Foundry & Machine Co. v. Hall, 121 Mass. 272; Katama Land Co. v. Jernegan, 126 Mass. 155; Franklin Glass Co. v. Alexander, 2 N. H. 380, 9 Am. Dec. 92; Odd Fellows' Hall Co. v. Glazier, 5 Har. (Del.) 172; Kennebec & Portland R. Co. v. Kendall, 31 Me. 470; Bel-fast & Moosehead Lake Ry. Co. v. Moore, 60 Me. 561.

Compare Bangor Bridge Co. v. McMahon, 10 Me. 678; Buckfield Branch R. Co. v. Irish, 39 Me. 44; Penobscot & Kennebec R. Co. v. Dunn, 39 Me. 587; York & Cumberland R. Co. v. Pratt, 40 Me. 447.

There is dictum to this effect in Connecticut & Passumpsic Rivers Bend Gas & Fuel Co., 48 Kan. 614. R. Co. v. Bailey, 24 Vt. 465, 58 Am.

Dec. 181, but it is mere dictum; and the contrary was held in Windsor Electric Light Co. v. Tandy, 66 Vt. 248, 44 Am. St. Rep. 838.

585 United States: Upton v. Tribilcock, 91 U. S. 45, 1 Cum. Cas. 824; Hawley v. Upton, 102 U. S. 314; Chubb v. Upton, 95 U. S. 665.

Alabama: Beene v. Cahawba & Marion R. Co., 3 Ala. 660; Selma & Tennessee R. Co. v. Tipton, 5 Ala. 787, 39 Am. Dec. 344; Gayle v. Cahawba & Marion R. Co., 8 Ala.

California: Mitchell v. Beckman, 64 Cal. 117; San Joaquin Land & Water Co. v. Beecher, 101 Cal. 70.

Connecticut: Hartford & New Haven R. Co. v. Kennedy, 12 Conn. 500; Danbury & Norwalk R. Co. v. Wilson, 22 Conn. 435.

Georgia: Branch Glass Works, 95 Ga. 573.

Peake v. Wabash R. Illinois: Co., 18 Ill. 88; Ionica & Petersburg R. Co. v. McNeely, 21 Ill. 71. Indiana: Heaston v. Cincinnati

& Ft. Wayne R. Co., 16 Ind. 275, 79 Am. Dec. 430; Miller v. Wild Cat Gravel Road Co., 52 Ind. 51.

Iowa: Nulton v. Clayton, 54 Iowa, 425, 37 Am. Rep. 213; Waukon & Mississippi R. Co. v. Dwyer, 49 Iowa, 121.

Kansas: McCormick v. Great Kentucky: Instone v. Frankfort tion, said the Kentucky court in an early case, the subscriber becomes ipso facto a member of the corporation, and the rights and immunities which attach to him in that capacity constitute a sufficient consideration to impose upon him a legal obligation to pay according to the terms upon which shares were authorized.' When, therefore, the corporation has been duly organized, the directors duly elected, and they have, as authorized by the act of incorporation, prescribed that an installment of a certain amount upon each share subscribed shall be paid by a certain day, and the subscriber has due notice thereof, he becomes legally liable to pay the amount of such installment upon the shares held by him; and whenever there is a legal liability, the law creates a promise upon which an action of assumpsit will lie.586

Effect of remedy by forfeiture or sale of shares.—The fact that the charter of a corporation or the general law gives it a special remedy against shareholders who are delinquent in the payment of assessments, by allowing it to forfeit or sell their shares, does not, if the charter or statute is merely affirmative, prevent it from maintaining an action of assumpsit on the express or implied promise of the shareholder to pay his sub-

Bridge Co., 2 Bibb, 576, 5 Am. Dec. 638; Fry v. Lexington & Big Sandy R. Co., 2 Metc. 314; Mt. Sterling Coal Road Co. v. Little, 14 Bush, 429.

Louisiana: Cucullu v. Union Ins. Co., 2 Rob. 573.

Hughes v. Antietam Maryland:

Mfg. Co., 34 Md. 316.

v. Arctic Michigan: Carson Mining Co., 5 Mich. 288; Dexter & Mason Plank Road Co. v. Millord, 3 Mich. 91.-

New York: Spear v. Crawford, 14 Wend. 20, 28 Am. Dec. 513; Lake Ontario, Auburn & N. Y. R. Co. v. Mason, 16 N. Y. 451; Rensselaer & Washington Plank Road Co. v. Barton, 16 N. Y. 457, note; Dayton v. Borst, 31 N. Y. 435; Phoenix Warehousing Co. v. Badger, 67 N. Y. 294.

Pennsylvania: Merrimac Mining Co. v. Levy, 54 Pa. St. 227, 93 Am. Dec. 697; Bavington v. Pittsburgh & Steubenville R. Co., 34 Pa. St. 358.

South Carolina: Columbia Corp. v. Harrison, 2 Mill. Const. 213.

Tennessee: Mobile & Ohio R. Co. v. Yandal, 5 Sneed, 294; East Tennessee & Virginia R. Co. v. Gammon, 5 Sneed, 566; Chase v. East Tennessee, Virginia & G. R. Co., 5 Lea, 415.

Vermont: Windsor Electric Light Co. v. Tandy, 66 Vt. 248, 44 Am. St. Rep. 838.

West Virginia: Kimmins v. Wilson. 8 W. Va. 584.

586 Instone v. Frankfort Bridge Co., 2 Bibb (Ky.) 576, 5 Am. Dec. scription, instead of pursuing the special remedy. In such a case, the special remedy is merely cumulative. 587 As we have

587 United States: Rockville & Washington Turnpike-Road Co. v. Maxwell, 2 Cranch, C. C. 451, Fed. Cas. No. 11,985.

Alabama: Beene v. Cahawba & Marion R. Co., 3 Ala. 660; Carlisle v. Cahawba & Marion R. Co., 4 Ala. 70; Selma & Tennessee R. Co. v. Tipton, 5 Ala. 787, 39 Am. Dec. 344; Tutwiler v. Tuskaloosa Coal, Iron & Land Co., 89 Ala. 391.

Lankershim Ranch California: Land & Water Co. v. Herberger, 82 Cal. 600; San Joaquin Land & Water Co. v. Beecher, 101 Cal, 70.

Denver Chamber of Colorado: Commerce v. Green, 8 Colo. App.

Connecticut: Hartford & New Haven R. Co. v. Kennedy, 12 Conn. 499; Mann v. Cooke, 20 Conn. 178. Florida: Barbee v. Jacksonville

& Alligator Plank Road Co., 6 Fla. 262; Kirksey v. Florida & Georgia Plank-Road Co., 7 Fla. 23, 68 Am. Dec. 426.

Georgia: Hightower v. Thornton, 8 Ga. 486, 52 Am. Dec. 412; Macon & Augusta R. Co. v. Vason, 57 Ga. 314.

Illinois: Klein v. Alton & Sangamon R. Co., 13 Ill. 514; Peoria & Oquawka R. Co. v. Elting, 17 Ill. 429; Raymond v. Caton, 24 Ill. 123 (where the contract of subscription provided for forfeiture).

Kentucky: Instone v. Frankfort Bridge Co., 2 Bibb, 576, 5 Am. Dec.

638.

Louisiana: Mexican Gulf Ry. Co. v. Viavant, 6 Rob. 305; New Orleans, Florida & H. Steamship Co. v. Briggs, 27 La. Ann. 318.

Maine: South Bay Meadow Dam Co. v. Gray, 30 Me. 547; Kennebec & Portland R. Co. v. Jarvis, 34 Me. 360.

Maryland: Hughes v. Antietam Mfg. Co., 34 Md. 316; Murphy v. Patapsco Ins. Co., 6 Md. 99.

Massachusetts: Worcester Turnpike Corp. v. Willard, 5 Mass. 80,

Turnpike Corp. v. Gould, 6 Mass. 40, 4 Am. Dec. 80; Taunton & South Boston Turnpike Corp. v. Whiting, 10 Mass. 327, 6 Am. Dec. 124; City Hotel v. Dickinson, 6 Gray, 686; Boston, Barre & G. A. R. Co. v. Wellington, 113 Mass. 79; Mechanics' Foundry & Machine Co. v. Hall, 121 Mass. 272.

Dexter & Michigan: Plankroad Co. v. Millerd, 3 Mich. 91: International Fair & Exposition Ass'n v. Walker, 83 Mich. 386, 88 Mich. 62; Atlantic Dynamite Co. v. Andrews, 97 Mich. 466.

Freeman v. Win-Mississippi:

chester, 10 Smedes & M. 577. New Hampshire: New New Hampshire Central R. Co. v. Johnson, 30 N. H. 390, 64 Am. Dec. 300; White Mountains R. Co. v. Eastman, 34 Jones, 39 N. H. 491; Shattuck v. Robbins, 68 N. H. 565.

New York: Goshen & Minisink Turnpike Road v. Hurtin, 9 Johns. 217, 6 Am. Dec. 273 (distinguishing and explaining Union Turnpike Co. v. Jenkins, 1 Caines, Cas. 381); Dutchess Cotton Manufactory v. Davis, 14 Johns. 238, 7 Am. Dec. 459; Small v. Herkimer Mfg. Co., 2 N. Y. 339; Burrows v. Smith, 10 N. Y. 566; Buffalo & New York City R. Co. v. Dudley, 14 N. Y. 336; Lake Ontario, Auburn & N. Y. R. Co. v. Mason, 16 N. Y. 451; Rensselaer v. Washington Plank Road Co. v. Barton, 16 N. Y. 457, note. North Carolina: Tar River Nav-

igation Co. v. Neal, 3 Hawks, 520.

Pennsylvania: Delaware Schuylkill Canal Navigation v. Sansom, 1 Binn. 70.

Greenville & South Carolina: Columbia R. Co. v. Cathcart, 4 Rich.

Tennessee: Stokes v. Lebanon & Sparta Turnpike Co., 6 Humph.

Vermont: Connecticut & Passumpsic Rivers R. Co. v. Bailey. 4 Am. Dec. 39; Andover & Medford 24 Vt. 465, 58 Am. Dec. 181; Windseen, however, in Maine, Massachusetts, and New Hampshire, there must be an express promise to pay the assessment in order that an action may be maintained.<sup>588</sup>

Whether or not an action can be maintained on a subscription after a sale or forfeiture of the shares for nonpayment of assessments is considered in a subsequent section.<sup>589</sup>

### § 493. Forfeiture or sale of shares.

A corporation has no power to forfeit or sell shares of its stock for nonpayment of assessments or calls, unless the power has been expressly conferred upon it by its charter or the general law, or by a provision in the articles of association, or otherwise by consent of the stockholders. Unless authorized, a majority of the stockholders cannot confer the power upon the corporation, as against a stockholder who does not assent, by enacting a by-law to such effect. It is perfectly competent, however, even in the absence of any provision in the char-

sor Electric Light Co. v. Tandy, 66 Vt. 248, 44 Am. St. Rep. 838.

Virginia: Brokenbrough v. James River & Kanawha Co., 1 Pat. & H. 94.

Washington: Puget Sound & Chehalis R. Co. v. Ouellette, 7 Wash. 265.

But it has been held that, where a statute prescribes the procedure to be followed in levying an assessment on stock, which includes publication of a notice stating the amount of the assessment, when stock will be delinquent for nonpayment thereof, and that any delinguent stock will be sold, and provides that on the day specified for declaring stock delinquent, or at any time thereafter, the directors may waive further proceedings to collect the assessments by sale of the stock, and elect to sue therefor, the provisions of the statute must be followed before an action can be brought to enforce personal liability for assessments. Shively v. Eureka T. Gold Mining Co., 129 Cal. 293.

588 See supra, this section.

589 Post, § 494.

Long Island R. Co., 19 Wend. (N. Y.) 37, 32 Am. Dec. 429; Budd v. Multnomah Street Ry. Co., 15 Or. 413, 3 Am. St. Rep. 169; Westcott v. Minnesota Mining Co., 23 Mich. 145; Minnehaha Driving Park Ass'n v. Legg, 50 Minn. 333; Gill v. Kentucky & C. Gold & Silver Min. Co., 7 Bush (Ky.) 635; Bordentown & South Amboy Turnpike Co. v. Imlay, 4 N. J. Law, 285; Downing v. Potts, 23 N. J. Law, 66; In re St. Lawrence Steamboat Co., 44 N. J. Law, 529; Edgerton Tobacco Mfg. Co. v. Croft, 69 Wis. 256; Copland v. Minong Mining Co., 33 Mich. 2; Cartwright v. Dickinson, 88 Tenn. 476, 17 Am. St. Rep. 910; Morris v. Metalline Land Co., 164 Pa. St. 326, 44 Am. St. Rep. 614. And see Kirk v. Nowill, 1 Term R. 118; Barton's Case, 4 De Gex & J. 46.

<sup>591</sup> Kirk v. Nowill, 1 Term R. 118; In re Election of Directors of Long Island R. Co., 19 Wend. (N. Y.) 37, 32 Am. Dec. 429. ter or general law, for a stockholder to expressly agree to a forfeiture or sale for nonpayment, as by a provision in the contract of subscription, or indorsed on the certificate of stock.<sup>592</sup> All the stockholders may undoubtedly pass a by-law, by unanimous vote, giving the corporation the right to forfeit or sell their shares. And even when a by-law to this effect is adopted without the unanimous consent of all the stockholders, those who do consent will not be heard to complain of a forfeiture or sale of their shares in accordance with its provisions.<sup>593</sup> Generally, the power to forfeit or sell the shares of delinquent stockholders is expressly conferred upon a corporation by its charter or the general law.\*

If a corporation is given a remedy in the alternative, either to forfeit shares for nonpayment of assessments, or to maintain an action, it cannot forfeit shares after it has brought an action and obtained a judgment. 594

When a statute giving a corporation the power to forfeit or sell shares for nonpayment of assessments, or the articles of association in pursuance thereof, prescribe the conditions under which, and the mode in which, the power shall be exercised, the prescribed conditions must exist, and the provisions of the statute as to the mode must be strictly complied with, or the sale or forfeiture will be invalid as against the stockholders, 595 although it may not be so as against the corporation. 596

592 See Raymond v. Caton, 24 Ill. 123; Weeks v. Silver Islet Consolidated Mining Co., 23 Jones & S. York & (N. Y.) 1; Lesseps v. Architects' Ritchie, Co. of New Orleans, 4 La. Ann.

593 Lesseps v. Architects' Co. of New Orleans, 4 La. Ann. 316.

\*See Elizabeth City Cotton Mills v. Dunstan, 121 N. C. 12, and other cases hereafter cited.

594 Giles v. Hutt, 3 Exch. 18. <sup>595</sup> Clarke v. Hart, 6 H. L. Cas. 633; Johnson v. Lyttle's Iron Agency, 5 Ch. Div. 687; Garden Gully United Quartz Mining Co. v.

Morris v. Metalline Land Co., 164 Pa. St. 326, 44 Am. St. Rep. 614; York & Cumberland R. Co. v. 40 Me. 425: Lewev's Island R. Co. v. Bolton, 48 Me. 451, 77 Am. Dec. 236; Portland, Saco & P. R. Co. v. Graham, 11 Metc. (Mass.) 1; Occidental Building & Loan Ass'n v. Sullivan, 62 Cal. 394; Budd v. Multnomah St. Ry. Co., 15 Or. 413, 3 Am. St. Rep. 169; Co., 15 Or. 415, 5 Am. St. Rep. 100, Downing v. Potts, 23 N. J. Law, 66; Mitchell v. Vermont Copper Mining Co., 47 How. Pr. (N. Y.) 218, 67 N. Y. 280; Eastern Plank Gully United Quartz Mining Co. v. Road Co. v. Vaughan, 20 Barb. (N. McLister, 1 App. Cas. 39; German-Y.) 155; Clise Investment Co. v. town Passenger Ry. Co. v. Fitler, Washington Savings Bank, 18 60 Pa. St. 124, 100 Am. Dec. 546; Wash. 8; Raht v. Sevier Mining &

If the charter of a corporation or a general law confers upon the corporation the power to enact by-laws providing for the sale or forfeiture of shares of delinquent stockholders, a valid by-law is an essential prerequisite to the power to declare a forfeiture or make a sale. A forfeiture or sale in pursuance of a mere resolution of the board of directors is invalid. 597

If the statute or articles expressly require the shares to be sold at public auction or at a particular place, a private sale, or a sale at a different place, is void. 598

A stockholder is entitled to reasonable notice before a sale or forfeiture of his shares for nonpayment of assessments, whether it is expressly required by the charter, statute, or by-laws, or not. 599 But it is generally expressly required. Any provision of the statute or articles of association as to notice of calls before a forfeiture or sale, or as to notice of the forfeiture or sale, etc., must be strictly followed.600 Thus, where articles of association provided that the directors of a corporation should have authority to make a requisition for payment of installments upon shares by giving thirty days' notice in newspapers published in the cities of Philadelphia and Detroit, and that after such time they might forfeit the shares of all persons failing to pay the installments, it was held that a forfeiture based upon a publication of such notice in one only of such cities was

Milling Co., 18 Utah, 290; Schwab v. Frisco Mining & Milling Co., 21

Utah, 258.
596 The corporation cannot treat · a forfeiture as invalid because of irregularity in declaring the same, and hold the stockholder liable as if no forfeiture had been declared. Patterson v. Brown & Campion Ditch Co., 3 Colo. App. 511; Austin's Case, 24 Law T. (N. S.) 932.

597 Budd v. Multnomah Street Ry. Co., 15 Or. 413, 3 Am. St. Rep.

599 Germantown Passenger Ry. Co. v. Fitler, 60 Pa. St. 124, 100 Am. Dec. 546; Rutland & Burling-ton R. Co. v. Thrall, 35 Vt. 536.

600 Johnson v. Lyttle's Iron Agency, 5 Ch. Div. 687; Watson v. Eales, 23 Beav. 294; Morris v. Metalline Land Co., 164 Pa. St. 326, 44 Am. St. Rep. 614, collecting cases; Lewey's Island R. Co. v. Bolton, 48 Me. 451, 77 Am. Dec. 236; Rutland & Burlington R. Co. v. Thrall, 35 Vt. 536; Mississippi, Ouachita & R. R. Co. v. Gaster, ouacnita & R. R. R. Co. v. Gaster, 20 Ark. 455; Lake Ontario, Auington Savings Bank, 18 Wash. 8. burn & N. Y. R. Co. v. Mason, 16 508 Portland, Saco & P. R. Co. v. N. Y. 451; Sands v. Sanders, 26 Graham, 11 Metc. (Mass.) 1; N. Y. 239; Lexington & West Cambewey's Island R. Co. v. Bolton, bridge R. Co. v. Staples, 5 Gray 48 Me. 451, 77 Am. Dec. 236. (Mass.) 520. void. 601 When the statute prescribes a certain notice, no other or further notice is necessary.602

Of course, in order that a forfeiture or sale of shares for nonpayment of calls or assessments may be valid, the shareholder must be in default. It follows that the calls or assessments must be valid, for this is necessary to put the shareholder in default. 603 A sale or forfeiture for nonpayment of several calls or assessments is invalid if one of the calls or assessments is invalid.604 If the amount legally due on the shares has been tendered to the corporation and refused, the shareholder is not in default, and a forfeiture or sale is invalid.605 But a tender of the amount due after a regular sale or forfeiture is too late to have any effect.606

In order that a forfeiture for nonpayment of a call may be voted, the board of directors by which the call was made and the forfeiture declared must have been a legally constituted board.607

### § 494. Effect of sale or forfeiture.

After shares have been regularly forfeited or sold for nonpayment of an assessment or call, the former owner is clearly no longer a stockholder, and he has no further interest or rights, as such, against the corporation. 608 If the sale or forfeiture is

601 Morris v. Metalline Land Co., 164 Pa. St. 326, 44 Am. St. Rep.

602 Germantown Passenger Ry. Co. v. Fitler, 60 Pa. St. 124, 100 Am. Dec. 546.

Notice by mail is sufficient if received, but not otherwise, unless expressly authorized. Elizabeth City Cotton Mills v. Dunstan, 121 N. C. 12. And see post, § 500.

Where a corporation has notice of the death of a member, it cannot bind his estate by posting to him at the address registered on its books a notice preliminary to forfeiting his shares for nonpayment of calls, although its articles pro-

post. Allen v. Gold Reefs of West Africa [1899] 2 Ch. 40.

603 Post, § 497 et seq. 604 Lewey's Island R. Co. v. Bolton, 48 Me. 451, 77 Am. Dec. 236; Stoneham Branch R. Co. v. Gould, 2 Gray (Mass.) 277.

605 Sweny v. Smith, L. R. 7 Eq. 324; Mitchell v. Vermont Copper Mining Co., 67 N. Y. 280.

606 Germantown Passenger Ry. Co. v. Fitler, 60 Pa. St. 124, 100 Am. Dec. 546.

607 Garden Gully United Quartz Mining Co. v. McLister, 1 App. Cas. 39; Moses v. Tompkins, 84

608 Sparks v. Proprietors of Livvide for service of such notices by erpool Water Works, 13 Ves. 428;

regular, a court of equity cannot relieve the stockholder by setting the same aside and restoring him to membership, even though he may tender the amount due.609

Since a stockholder is no longer such after a regular sale or forfeiture of his shares for nonpayment of assessments, he is not afterwards subject to any statutory liability to creditors on the insolvency of the corporation. 610

Whether or not a corporation or its creditors can maintain an action to recover a balance due on a subscription after the shares have been regularly forfeited or sold for nonpayment of an assessment depends upon the terms of the statute authorizing the forfeiture or sale, and the effect thereof. As a general rule, after the shares are regularly forfeited for nonpayment of an assessment, and belong to the corporation, so that it may reissue the same, there is no further liability on the part of the subscriber, either to the corporation or to its creditors in case of insolvency. 611 The right to maintain an action, however, in such a case, notwithstanding the forfeiture, may be expressly

Germantown Passenger Ry. Co. v. Fitler, 60 Pa. St. 124, 100 Am. Dec. 546; St. Louis & S. Coal & Mining Co. v. Sandoval Coal & Mining Co., 116 Ill. 170.

When a corporation increases its capital stock, and afterwards reduces the same to the original amount, refunding the amounts paid by the subscribers for the increased stock, a subscriber for such stock, whose shares have been duly forfeited before the reduction for nonpayment of an installment is not entitled to the refund of what he has paid. Congress & Empire Spring Co. v. Knowlton, 103 U. S. 49; Knowlton v. Congress & Empire Spring Co., 57 N. Y. 518.

609 Sparks v. Proprietors of Liverpool Water Works, 13 Ves. 428; Germantown Passenger Ry. Co. v. Fitler, 60 Pa. St. 124, 100 Am. Dec.

610 Mills v. Stewart, 41 N. Y. 384. See, also, Macauly v. Robinson, 18 La. Ann. 619.

611 Ashton v. Burbank, 2 Dill. 435, Fed. Cas. No. 582; Small v. Herkimer Manufacturing & Hydraulic Co., 2 N. Y. 330 (reversing 21 Wend. 273); Mills v. Stewart, 41 N. Y. 384; Northern R. Co. v. Miller, 10 Barb. (N. Y.) 260; Rutland & Burlington R. Co. v. Thrall, 35 Vt. 536; Macauly v. Robinson, 18 La. Ann. 619; Athol & Enfield R. Co. v. Inhabitants of Prescott. 110 Mass. 213; Mechanics' Foundry & Machine Co. v. Hall, 121 Mass. 272; Mandel v. Swan Land & Cattle Co., 154 Ill. 177, 45 Am. St. Rep. 124; Allen v. Montgomery R. Co., 11 Ala. 437; Macon & Augusta R. Co. v. Vason, 57 Ga.

Where a corporation exercises its power to forfeit the stock of a subscriber for the nonpayment of a call, it cannot afterwards recover on a note given by him for a previous unpaid assessment on the stock. Ashton v. Burbank, 2 Dill. 435, Fed. Cas. No. 582.

conferred by the charter of the corporation, or by a general law.<sup>612</sup>

It has been held that the right to maintain an action against a delinquent stockholder after a valid forfeiture of his shares for nonpayment of an assessment cannot be conferred upon a corporation by a mere by-law.<sup>613</sup> It is otherwise, however, if it is expressly given the power to adopt by-laws providing for the forfeiture or sale of shares.<sup>614</sup>

In any event, a forfeiture, to relieve a stockholder from liability to creditors, must have been in good faith. If there was fraud or collusion, the stockholder remains liable. 615

There is dictum to the effect that if shares are sold for nonpayment of assessments (not forfeited and reacquired by the corporation), the corporation has no further remedy against the subscriber, and if the amount realized from the sale is insufficient to pay the amount due on the shares, the corporation cannot maintain an action for the deficiency. 616 This proposition, however, cannot be sustained unless the statute clearly shows an intent to make the sale of the shares and an action on the subscription alternative remedies. As a rule, when a statute authorizes a corporation to sell the shares of delinquent subscribers, it merely gives it a security in the nature of a pledge or mortgage. If the sale should bring more than is due on the shares, the shareholder would be entitled to the surplus. And if it brings less, he remains liable for the deficiency, and the corporation may maintain an action therefor, notwithstanding the sale. 617 When the charter or statute, however, allows the

612 Great Northern Ry. Co. v. Kennedy, 4 Exch. 417; Creyke's Case, 5 Ch. App. 63; Mandel v. Swan Land & Cattle Co., 154 Ill. 177, 45 Am. St. Rep. 124; Stokes v. Lebanon & Sparta Turnpike Co., 6 Humph. (Tenn.) 241; Mann v. Cooke, 20 Conn. 178.

613 Mandel v. Swan Land & Cattle Co., 154 Ill. 177, 45 Am. St. Rep. 124

614 Elizabeth City Cotton Mills v. Dunstan, 121 N. C. 12, 61 Am. St. Rep. 654.

615 Walters' Second Case, 3 De Gex & S. 244; Stanhope's Case, 1 Ch. App. 161; Stewart's Case, 1 Ch. App. 511; Spackman v. Evans, L. R. 3 H. L. 171; Slee v. Bloom, 19 Johns. (N. Y.) 456, 10 Am. Dec. 273; Mills v. Stewart, 41 N. Y. 384. 616 Instone v. Frankfort Bridge Co., 2 Bibb (Ky.) 576, 5 Am. Dec. 638.

617 Carson v. Arctic Mining Co.,
5 Mich. 288; Merrimac Mining Co.
v. Bagley, 14 Mich. 501; Great
Northern Ry. Co. v. Kennedy, 4

corporation to either forfeit or sell shares for nonpayment of assessments, or to maintain an action to recover the amount of the assessment, making the remedy by forfeiture or sale an. alternative remedy, the corporation, after declaring a forfeiture or making a sale, has no further remedy. It cannot afterwards maintain an action to recover assessments. 618

The corporation is certainly not precluded from maintaining an action to recover assessments on subscriptions by the fact that it has so far pursued the statutory remedy by way of sale of the shares as to exhibit or offer them for sale, if no sale has Nor is it precluded by a mere resolution to forbeen made. 619 feit shares, where they have not yet been forfeited.620

#### § 495. Remedy in case of unauthorized or irregular forfeiture or sale.

If a corporation sells or forfeits shares when it has no power to do so, or without complying with charter or statutory requirements, or otherwise wrongfully, the shareholder may maintain a suit in equity to set the forfeiture or sale aside, and compel the corporation to admit him to his rights as a stockholder, and, in case of a sale, to enjoin a transfer of the shares to the purchaser. 621 Or he may treat the forfeiture or sale as a con-

Exch. 417; Danbury & Norwalk R. Co. v. Wilson, 22 Conn. 435; Succession of Thomson, 46 La. Ann. 1074. And see the dictum in Small v. Herkimer Manufacturing & Hydraulic Co., 2 N. Y. 330. See, also, Elizabeth City Cotton

Mills v. Dunstan, 121 N. C. 12, 61 Am. St. Rep. 654, where the sale was under a by-law which the corporation was authorized to enact. 618 Edinburgh, Leith & N. Ry. Co. v. Hebblewhite, 6 Mees. & W.

707; Inglis v. Great Northern Ry. Co., 1 Macq. H. L. Cas. 112; Giles v. Hutt, 3 Exch. 18; Great Northern Ry. Co. v. Kennedy, 4 Exch.

Co., 2 Bibb (Ky.) 576, 5 Am. Dec. 638; Macon & Augusta R. Co. v. ularly sold for nonpayment of as-Vason, 57 Ga. 314; Grays v. Lynch- sessments thereon cannot be main-

burg & S. Turnpike Co., 4 Rand. (Va.) 578.

620 Hays v. Franklin County Lumber Co., 35 Neb. 511. And see Macon & Augusta R. Co. v. Vason, 57 Ga. 314; Minnehaha Driving Park Ass'n v. Legg, 50 Minn. 333. 621 Sweny v. Smith, L. R. 7 Eq.

324; Ormsby v. Vermont Copper Mining Co., 56 N. Y. 623; Mitchell v. Vermont Copper Mining Co., 67

A stockholder may waive the right to have a sale for nonpayment of assessments set aside for irregularities, and he does so by n Ry. Co. v. Kennedy, 4 Exch. unreasonable delay in exercising 7. the right. Raht v. Sevier Mining 619 Instone v. Frankfort Bridge & Milling Co., 18 Utah, 290.

An action to recover stock irreg-

version of his stock by the corporation, and maintain an action of trover to recover his damages. 622 In a proper case he may sue in equity, tendering payment of any assessments that may be due. 623 to enjoin a threatened forfeiture or sale. 624

A stockholder whose stock has been illegally forfeited cannot sue the corporation for a specific interest in the corporate property. 625

Laches.—A stockholder whose shares have been irregularly, but in good faith, forfeited for nonpayment of an assessment, may be estopped by laches from insisting upon a reinstatement entitling him to share in the subsequent profits of the company, if, with full knowledge of the forfeiture, he has stood by and allowed the others to contribute the funds necessary for the business of the company. 626 There is no estoppel, however, where the forfeiture is void, the stockholder not having been in default, and where the company is not engaged in a business requiring contributions from its members to sustain its existence or business, and there has been no intentional abandonment, or "lying by for chances."627

# § 496. Set-off and counterclaim by subscriber.

When a subscriber is sued upon his subscription by the corporation, he may set up, by way of set-off or counterclaim, a

tained without compliance with a statute requiring payment or tender of the sum for which the stock was sold, with interest thereon. Raht v. Sevier Mining & Milling Co., 18 Utah, 290.

 622 Budd v. Multnomah St. Ry.
 Co., 15 Or. 413, 3 Am. St. Rep. 169; Allen v. American Building & Loan Ass'n, 49 Minn. 544, 32 Am. St. Rep. 574; Carpenter v. American Building & Loan Ass'n, 54 Minn. 403, 40 Am. St. Rep. 345; ante. § 379.

see ante, § 379(c).

623 Burham v. San Francisco Fuse Mfg. Co., 76 Cal. 26.

624 Schuetz v. German-American Real Estate Co., 21 App. Div. (N. Y.) 163; Moore v. New Jersey Lighterage Co., 25 Jones & S. (N. Y.) 1, 5 N. Y. Supp. 192; Green v. Abietine Medical Co., 96 Cal. 322. 625 Smith v. Maine Boys Tunnel

Co., 18 Cal. 111. 626 Prendergast v. Turton, 1 Younge & C. 109; Clarke v. Hart, 6 H. L. Cas. 649; Rule v. Jewell, 18 Ch. Div. 660; Raht v. Sevier Mining & Milling Co., 18 Utah, 290. tte, § 379.

As to the measure of damages, 164 Pa. St. 326, 44 Am. St. Rep. 614. See, also, Garden Gully United Quartz Mining Co. v. McLister, 1 App. Cas. 39, 55.

debt due him from the corporation.<sup>628</sup> By the weight of authority, however, as we shall see in a subsequent chapter, he cannot do so when the corporation is insolvent, and it is sought to enforce the subscription for the benefit of its creditors.<sup>629</sup>

VII. CALLS OR ASSESSMENTS ON UNPAID SUBSCRIPTIONS.

§ 497. In general.—If a subscription is in terms payable, not at a time or times certain, but as may be required by the directors or stockholders, a valid call is necessary to put a subscriber in default, and entitle the corporation to maintain an action against him, or forfeit or sell his shares; but no call is necessary when a subscription is payable at once, or at a fixed time in the future, or when it has been repudiated. A call is not valid unless made by the authority (or ratified), and in the mode, if any, prescribed by the charter, articles of association, or general law. In the absence of provision to the contrary, it is to be made by the board of directors.

By the weight of authority, notice of a call is not necessary unless it is expressly required. But where the charter, articles of association, or general law requires notice, or notice of a particular kind, etc., a subscriber cannot be put in default without a strict compliance therewith, unless he has actual notice.

Definitions.—The term "call," with reference to subscriptions to the capital stock of a corporation, is used in several senses. Ordinarily it is used merely to designate the resolution or declaration of the board of directors or other authority by which the whole or a part of unpaid subscriptions are made payable. 1st is also used to designate both this formal resolution or declaration, and the notice thereof or demand of payment, and other steps which may be required to render subscriptions payable, or to designate the time when the payment is

<sup>628</sup> Barnett's Case, L. R. 19 Eq. 449; Bausman v. Denny, 73 Fed. 69; Singer v. Given, 61 Iowa, 93; Boulton Carbon Co. v. Mills, 78 Iowa, 460; Agate v. Sands, 73 N. Y. 620.

<sup>620</sup> Post, chapter xxv.

<sup>630</sup> See Braddock v. Philadelphia, Marlton & M. R. Co., 45 N. J. Law, 363; Heaston v. Cincinnati & Ft. Wayne R. Co., 16 Ind. 275, 79 Am. Dec. 430; Spangler v. Indiana & Illinois Central Ry. Co., 21 Ill. 276; Newry & Enniskillen Ry. Co. v. Edmunds, 2 Exch. 118.

due. "The word 'call,' " said Parke, B., in an English case, "is capable of three meanings. It may either mean the resolution, or its notification, or the time when it becomes payable. It must mean either one of these three."631

The term "assessment," with reference to unpaid subscriptions, means the same thing as the term "call," the two terms being often used interchangeably. 632 This term, however, is also used to designate payments required to be made by stockholders over and above the par value of their shares, either to provide additional funds for the use of the corporation, or to pay creditors upon the insolvency of the corporation. 633 While the term "call," therefore, is properly applied to unpaid subscriptions, the term "assessment" applies both to unpaid and to full-paid stock.634

### § 498. When calls are necessary.

Whether or not a call is necessary to render a subscriber liable to an action on his subscription depends upon the terms of his contract of subscription, and the provisions of the charter of the corporation, general law, articles of association, and bylaws of the corporation, entering into and forming a part of his contract. No call is necessary when a subscription is payable, not upon call or demand by the directors or stockholders, but immediately, or on a specified day, or on or before a specified day, or when it is payable in installments at specified times. such cases it is the duty of the subscriber to pay the subscription or installment thereof as soon as it is due, without any call or demand, and, if he fails to do so, an action may be brought at any time.635

<sup>631</sup> Ambergate, Nottingham & B. & E. J. Ry. Co. v. Mitchell, 4 Exch. 540. See, also, Germania Iron Mining Co. v. King, 94 Wis. 439; Queen v. Londonderry & Coleraine Ry. Co., 13 Q. B. 998.

<sup>632</sup> See Budd v. Multnomah Street Ry. Co., 15 Or. 413, 3 Am. Street Ry. Co., 15 Or. 413, 3 Am. 625 New Albany & Salem R. Co. St. Rep. 169; Penobscot R. Co. v. v. McCormick, 10 Ind. 499, 71 Am.

<sup>40</sup> Me. 172, 63 Am. Dec. 654; Great Western Telegraph Co. v. Burnham, 79 Wis. 47, 24 Am. St. Rep. 698.

<sup>633</sup> Ante, § 402; post, chapter xxv.

<sup>634</sup> Omo v. Bernart, 108 Mich. 43. White, 41 Me. 512, 66 Am. Dec. Dec. 337; New Albany & Salem 275; Penobscot R. Co. v. Dummer, R. Co. v. Pickens, 5 Ind. 247; Estell

Generally, however, subscriptions are not thus made payable immediately or at specified times, but are subject to call. subscriptions are expressly or impliedly made payable upon call or demand by the directors or stockholders, either by the terms of the subscription paper itself, or by the charter of the corporation, or the general law, or articles of association, or by an authorized by-law adopted by the corporation prior to the subscription, a valid call by the directors or a majority of the stockholders, as the case may be, is a condition precedent to any liability on the subscription, and to the right of the corporation to maintain an action thereon,636 or to set up the subscription

Mason, 16 N. Y. 451; Phoenix Warehousing Co. v. Badger, 67 N. Y. 294; Northwood Union Shoe Co. v. Pray, 67 N. H. 435; Waukon & Mississippi R. Co. v. Dwyer, 49 Iowa, 121.

Although a statute may provide that no assessment shall exceed ten per cent. of the amount of the capital stock of a corporation, except that, if the whole has not been paid up, and the corporation is unable to meet its liabilities, the assessment may be for the full amount of the unpaid subscriptions, an agreement of subscription, by which the subscribers agree that the amounts subscribed by them shall be due and payable on the formation of the corporation and the issue of the stock, gives rise, on such formation, to a cause of action in favor of the corporation for the full amount, without any assessment or call, and although the money may not be then needed to satisfy liabilities of the corporation. Marysville Electric Light & Power Co. v. Johnson, 93 Cal. 538, 27 Am. St. Rep. 215.

638 Grissell's Case, 1 Ch. App.
528; Bank of South Australia v.
Abrahams, L. R. 6 P. C. 265; Seymour v. Sturgess, 26 N. Y. 134; property in payment of a subscrip-Glenn v. Howard, 65 Md. 40; tion may be maintained without Spangler v. Indiana & Illinois Cen-

v. Knightstown & Middletown tral Ry. Co., 21 Ill. 276; Banet v. Turnpike Co., 41 Ind. 174; Ruse v. Alton & Sangamon R. Co., 13 Ill. Bromberg, 88 Ala. 619; Lake On- 504; Great Western Telegraph Co. Co. v. Moore, 84 Ill. 575; South Georgia & Florida R. Co. v. Ayres, 56 Ga. 230; North & South St. R. Co. v. Spullock, 88 Ga. 283; Braddock v. Philadelphia, Marlton & M. R. Co., 45 N. J. Law, 363; Grosse Isle Hotel Co. v. Panson, 42 N. J. Law, 10, 43 N. J. Law, 442; Ruse v. Bromberg, 88 Ala. 619; Alabama & Florida R. Co. v. Rowley, 9 Fla. 508; New England Fire Ins. Co. v. Haynes, 71 Vt. 306, 76 Am. St. Rep. 771; Granite Roofing Co. v. Michael, 54 Md. 65; Ventura & Ojai Valley Ry. Co. v. Hartman, 116 Cal. 260; Halsey Fire-Engine Co. v. Donovan, 57 Mich. 318; Roberts v. Mobile & Ohio R. Co., 32 Miss. 373; Purton v. New Orleans & Carrollton R. Co., 3 La. Ann. 199; Washington Savings Bank v. Butchers' & Drovers' Bank, 107 Mo. 133, 28 Am. St. Rep. 405.

A call is not rendered unnecessary by reason of the fact that the stock, the subscription for which it is sought to enforce, was issued for property, and the transaction is attacked on the ground of fraud. Granite Roofing Co. v. Michael, 54

by way of set-off or counterclaim in an action by the subscriber.637 A call is necessary, for example, in the case of subscriptions payable "in such installments and at such times as may be decided by a majority of the stockholders, or board of directors. ''638

A call may be necessary to put a subscriber in default on a note given in payment of his subscription. It is necessary where the note is in terms "payable in such installments and at such time or times as the directors may require," etc. 639 when a note given for a subscription is payable absolutely on a day certain, no call is necessary before an action thereon by the corporation, or by an assignee in bankruptcy.640

If a subscriber repudiates his subscription, no call is necessary to render him liable to an action. 641 Nor is any other call necessary in the case of a subscription after a valid call has once been made.642

The necessity for calls when the corporation is insolvent and subscriptions are enforced for the benefit of creditors is considered in a subsequent chapter. 643

# Validity and sufficiency of calls.

(a) In general.—The validity of calls upon unpaid subscriptions is determined by the laws of the state or country in which the corporation is located.644

mand of performance. Cheraw & nonpayment of a subscription un-Chester R. Co. v. Garland, 14 S. C. less there has been a valid call. 63; Ohio, Indiana & I. R. Co. v. Cramer, 23 Ind. 490.

637 Holt v. Holt Electric Storage Co., 79 Fed. 597.

638 North & South St. R. Co. v. Spullock, 88 Ga. 283; Grissell's Case, 1 Ch. App. 528; and other cases in the note preceding.

Under a statute providing that all subscriptions shall be paid in such installments and at such times as the directors may require, and, if default be made in any payment, the person in default shall pay a certain additional amount, the penalty cannot be collected for ney, 61 Fed. 41.

Blair v. Wilson, 15 Pa. Super. Ct.

639 New England Fire Ins. Co. v. Haynes, 71 Vt. 306, 76 Am. St. Rep. 771. And see Lamar Ins. Co. v. Moore, 84 Ill. 575.

640 Ruse v. Bromberg, 88 Ala.

641 Cass v. Pittsburg, Virginia & C. Ry. Co., 80 Pa. St. 31.

642 Pike v. Bangor & Calais Shore Line R. Co., 68 Me. 445.

643 See post, chapter xxv.

644 American Pastoral Co. v. Gur-

(b) By whom made.—Calls are not valid, and cannot be enforced, unless they are made by the proper authority.645 In the absence of express provisions on the subject, they may and must be made by the board of directors as the managing agents of the corporation.646 If the statute merely authorizes the stockholders to make calls, it does not exclude the power of the directors to make them.647

If the charter or articles of association prescribe who shall exercise the power to make calls, the provision is mandatory, and the power cannot be validly exercised by any other person or persons.648 But if the power is exercised by others than the prescribed authority, their action may be adopted or ratified, for in such a case it becomes the action of the proper authoritv.649

As a general rule, the power cannot be delegated by the authority in which it is vested, as by the board of directors to the president or treasurer, for example. 650 It has been held, however, that when the power to make calls is vested in the stockholders, they may delegate the power to the directors.651

If a call is made by persons assuming to act as directors, but who are not directors, either de jure or de facto, it is necessarily void. In some of the cases it has been held that a valid call cannot be made by directors de facto merely, but that the board must be a legal board. 652 By the weight of authority, however,

Westcott, 14 Gray (Mass.) 440; New Jersey Midland Ry. Co. v. Strait, 35 N. J. Law, 322; and other cases in the notes following.

848 Ambergate, Nottingham & B. & E. J. Ry. Co. v. Mitchell, 4 Exch. 540; Budd v. Multnomah Street Ry. Co., 15 Or. 413, 3 Am. St. Rep.

647 Ambergate, Nottingham & B. & E. J. Ry. Co. v. Mitchell, 4 Exch.

645 People's Mutual Ins. Co. v. phis Gayoso Gas Co., 9 Heisk. (Tenn.) 545.

650 Rutland & Burlington R. Co. v. Thrall, 35 Vt. 536; Banet v. Alv. Thrail, 35 vt. 536; Banet v. Alton & Sangamon R. Co., 13 Ill. 504; Farmers' Mutual Fire Ins. Co. v. Chase, 56 N. H. 341; Monmouth Mutual Fire Ins. Co. v. Lowell, 59 Me. 504; Pike v. Bangor & Calais Shore Line R. Co., 68 Me. 445; Silver Hook Road v. Greene, 12 R. I. 164.

651 Rives v. Montgomery South

648 People's Mutual Ins. Co. v. Plank-Road Co., 30 Ala. 92.
Westcott, 14 Gray (Mass.) 440; Contra, Ex parte Winsor, 3
Moses v. Tompkins, 84 Ala. 613.
649 Rutland & Burlington R. Co.
v. Thrall, 35 Vt. 536; Read v. Mem613. And see People's Mutual Ins.

in this country, at least, a call by a *de facto* board of directors is valid.<sup>653</sup>

When a call is made by the board of directors, a quorum must be present, or the call will be void. 654

(c) Time of making call—Conditions precedent.—Of course, a call for payment of a subscription, or a part thereof, cannot be made if payment is not yet due according to the express and implied terms of the contract. It follows that no call can be made upon a subscription until performance or fulfillment of all express or implied conditions precedent to liability thereon, as explained in a former section. 655

As we have seen, it is an implied condition precedent to liability on a subscription, unless there is something to show a contrary intention, and except so far as may be necessary for payment of contemplated preliminary expenses, that the corporation shall have complied with all conditions precedent to the right to commence business, and until it has done so, no call can be made except for payment of preliminary expenses. When, as will be explained in a subsequent section, it is a condition precedent, express or implied, that the full amount of the capital stock, or a certain percentage thereof, shall be subscribed before the subscribers shall be liable on their subscriptions, an assessment or call other than for necessary preliminary expenses is invalid, if made before performance of the condition, 657 un-

Co. v. Westcott, 14 Gray (Mass.)

This is the rule in England. Garden Gully United Quartz Mining Co. v. McLister, 1 App. Cas. 39; Swansea Dock Co. v. Levien, 20 L. J. Exch. 447; Howbeach Coal

Co. v. Teague, 5 Hurl. & N. 151.
653 Chandler v. Sheep Rock Mining & Milling Co., 15 Utah, 434;
Fairfield County Turnpike Co. v. Thorp, 13 Conn. 173; Covington,
C. C. & J. Plank-Road Co. v. Moore,
3 Ind. 510; Eakright v. Logansport & Northern Indiana R. Co.,
13 Ind. 404; Johnson v. Crawfordsville, F. K. & Ft. W. R. Co., 11
Ind. 280; Atherton v. Sugar Creek
& P. Turnpike Co., 67 Ind. 334;

Steinmetz v. Versailles & O. Turnpike Co., 57 Ind. 457; Macon & Augusta R. Co. v. Vason, 57 Ga. 314; San Joaquin Land & Water Co. v. Beecher, 101 Cal, 70.

654 Bottomley's Case, 16 Ch. Div. 681; Price v. Grand Rapids & Indiana R. Co., 13 Ind. 58; Hamilton v. Grand Rapids & Indiana R. Co., 13 Ind. 347.

655 Ante, § 455 et seq.

656 Anvil Mining Co. v. Sherman, 74 Wis. 226; Salem Mill Dam Corp. v. Ropes, 6 Pick. (Mass.) 23, 2 Keener's Cas. 1245; Id., 9 Pick. 187, 19 Am. Dec. 363.

<sup>657</sup> Salem Mill Dam Corp. v. Ropes, 6 Pick. (Mass.) 23, 2 Keen-

less the condition has been waived by the subscriber objecting, or he is estopped to set up its nonperformance.658 And it is none the less so because of the fact that the condition was performed on the same day on which the assessment was made, if it was not performed until after the dissolution of the meeting of the directors at which it was made. 659

(d) Purpose of call and necessity therefor.—Undoubtedly, calls or assessments upon unpaid subscriptions cannot be made except for the legitimate purpose of the corporation. They cannot be made to raise money to be used or invested for an unauthorized purpose. 660 It will be presumed, however, that they were made for a legitimate purpose unless the contrary appears. 661 If they are made for a corporate purpose, they are not rendered invalid because the corporation owes no debts, or has sufficient property to pay its debts, or because contracts which it has made are illegal, and not enforceable against it.662 The necessity for a call is to be determined by the directors or other authority vested with the power to make calls, and is not open to question by the stockholders.663

er's Cas. 1245; Id., 9 Pick. 187, 19 Am. Dec. 363; Stoneham Branch R. Co. v. Gould, 2 Gray (Mass.) 277; Anvil Mining Co. v. Sherman, 74 Wis. 226; Ventura & Ojai Valley Ry. Co. v. Hartman, 116 Cal. 260. And see post, § 505.

An error in making a call upon subscriptions before performance of a condition precedent prescribed in the same may be corrected by making another call after performance of the condition. Philadelphia & West Chester R. Co. v. Hickman, 28 Pa. St. 318.

658 Post. § 507.

659 Stoneham Branch R. Co. v. Gould, 2 Gray (Mass.) 277.

660 See Penobscot R. Co. v. White, 41 Me. 512, 66 Am. Dec. 257; Habershon's Case, L. R. 5 Eq.

661 Penobscot R. Co. v. White, 41 Me. 512, 66 Am. Dec. 257.

662 Penobscot R. Co. v. White, 41 Me. 512, 66 Am. Dec. 257; Visa-lia & Tulare R. Co. v. Hyde, 110

"The right to make assessments cannot be made to depend upon any actual indebtedness existing at the time, nor defeated by any apparent indebtedness incurred under a contract which was void." Penobscot R. Co. v. White, 41 Me. 512, 66 Am. Dec. 257.

663 Bailey v. Birkenhead, Lancashire & C. J. Ry. Co., 12 Beav. 433; Budd v. Multnomah St. Ry. Co., 15 Or. 413, 3 Am. St. Rep. 169, citing Chouteau Ins. Co. v. Floyd, 74 Mo. 286; Judah v. American Live Stock 257; Habershon's Case, L. R. 5 Eq. Ins. Co., 4 Ind. 333. And see Great 286; Bank of China, Japan & The Straits v. Morse, 44 App. Div. (N. 162 U. S. 329; Visalia & Tulare R. Y.) 435.

The resolution of the directors need not recite or expressly show that the call is made for a corporate purpose, or that any demand of the business of the corporation requires that subscriptions shall be paid.664

(e) Mode of making calls.—In order that assessments or calls may be valid, they must be made in the manner, if any, prescribed by the charter, articles of association, or by-laws of the corporation, 665 unless a different mode is authorized by the terms of the contract of subscription.666

When subscriptions are payable simply upon call of the directors, it is for them to determine how they shall be paid, and they may call for payment either in full at one time, or in installments.667 When subscriptions stipulate that assessments shall not exceed a certain sum on each share at one time, several assessments may be voted at the same time, provided no greater sum than the amount limited is made payable on each share at one time, 668

No particular formalities are necessary unless expressly prescribed. Subject to special provisions, all that is necessary on the part of the board of directors to make a valid call is "that there should be some act or resolution which evinces or shows a

664 Budd v. Multnomah St. Ry. by-laws of the company made un-Co., 15 Or. 413, 3 Am. St. Rep. 169, 94 Wis. 439; Raht v. Sevier Mining & Milling Co., 18 Utah, 290.

666 Where a subscriber by his contract agrees to pay upon the call of the directors "at such times and in such manner as may be determined by" them, it is not necessary that the directors shall make calls or assessments on his stock in the mode prescribed by the charter of the corporation or the general law. California Southern Hotel Co. v. Callender, 94 Cal. 120, 28 Am. St. Rep. 99.

Where a subscription provides for payment of calls thereon "in conformity with the general incorporating law of the state, and the 35 Vt. 536.

der the same," the amount for 665 People's Mutual Ins. Co. v. which a call may be made will not Westcott, 14 Gray (Mass.) 440; necessarily be controlled by the Germania Iron Mining Co. v. King, general law, if the by-law prescribe a different rule. Stone v. Great Western Oil Co., 41 Ill. 85.

667 North Western Ry. Co. v. Mc-Michael, 6 Exch. 273; Ross v. Lafayette & Indianapolis R. Co., 6 Ind. 297; Haun v. Mulberry & Jefferson Gravel Road Co., 33 Ind. 103; Fox v. Allensville, C. S. & V. Turnpike Co., 46 Ind. 31; Hays v. Pittsburgh & Steubenville R. Co., 38 Pa. St. 81; Spangler v. Indiana & Illinois Central Ry. Co., 21 Ill. 276; Stone v. Great Western Oil Co., 41 Ill. 85.

668 Penobscot R. Co. v. Dummer, 40 Me. 172, 63 Am. Dec. 654; Rutland & Burlington R. Co. v. Thrall, clear official intent to render due and payable a part or all the unpaid subscription."<sup>669</sup> If there is such an act or resolution, and statutory requirements are substantially complied with, the call will not be rendered void by mere irregularities or informalities.<sup>670</sup>

Of course there must be some definite act or resolution to constitute a call, and not a mere conversation among the directors, or a mere declaration of an intention to make a call in the future.<sup>671</sup> The resolution or declaration must be sufficiently definite and certain to be capable of enforcement, and either the resolution or declaration, or the notice thereof, must fix the time and mode of payment in express terms, or by clear implication.<sup>672</sup> It has been held, however, that if the notice of a call definitely fixes the time and place of payment, and the person to

669 Budd v. Multnomah St. Ry. Co., 15 Or. 413, 3 Am. St. Rep. 169. A formal direction by the board

A formal direction by the board of directors to the president or treasurer to collect unpaid subscriptions has been held to be a call. Braddock v. Philadelphia, Marlton & M. R. Co., 45 N. J. Law, 363.

670 In re British Sugar Refining Co., 3 Kay & J. 408; Macon & Augusta R. Co. v. Vason, 57 Ga. 314; Hays v. Pittsburgh & Steubenville R. Co., 38 Pa. St. 81; Fox v. Allensville, C. S. & V. Turnpike Co., 46 Ind. 31.

Unless it is expressly required, an assessment or call by the directors' need not be signed by them. North River Meadow Co. v. Shrewsbury Christ Church, 22 N. J. Law, 424, 53 Am. Dec. 258.

671 Calls for payments of subscriptions to the capital stock of a corporation, payable "as the directors may direct," cannot be made by mere street conversations between the president and directors, in which they agree that the former may call in subscriptions as needed. Branch v. Augusta Glass Works, 95 Ga. 573.

672 Rutland & Burlington R. Co. Am. Dec. 430.

v. Thrall, 35 Vt. 536; Heaston v. Cincinnati & Ft. Wayne R. Co., 16 Ind. 275, 79 Am. Dec. 430.

A resolution by the directors of a corporation, requiring subscribers to its stock to pay a stated sum on their shares within a certain time, either in cash or by a promise to pay in the form of a land contract or contracts, whereupon stock is to become full-paid, is too indefinite to support an action against a subscriber for nonpayment of the sum called for. North Milwaukee Town Site Co. v. Bishop, 103 Wis. 492, 45 L. R. A.

A resolution of the board of directors that the stockholders "are hereby required to pay an installment of 10 per cent. every thirty days, on all cash subscriptions, until the whole subscriptions are paid; and that due notice thereof be given," etc., is not open to the objection that it is too vague, indefinite, and uncertain, or that it does not fix a definite time for payment. It shows a call for payment of an installment in thirty days from date, and every thirty days afterwards. Heaston v. Cincinnati & Ft. Wayne R. Co., 16 Ind. 275, 79

whom payments are to be made, it is no objection that the declaration or resolution does not do so.673 Indeed, the place of payment need not be specified at all, either in the call or in the notice, for if no place is fixed, payment is to be made at the office of the corporation.674

Even where iregularities are material, and would ordinarily invalidate a call, they may be waived by the stockholders.675 or a stockholder may be estopped by having participated as a stockholder or director in making the call, 676 or they may be cured, and the objection obviated by making a new call.677

(f) Inequality.—Unless some of the stockholders have already paid more on their subscriptions than others, a call must be made on all alike, or it will be void. Any call or assessment which requires some of the stockholders to pay a higher rate than the others, or which is otherwise unequal or partial, will not be enforced.678 This principle does not prevent a call which is

673 Great North of England Ry. Co. v. Biddulph, 7 Mees, & W. 243; American Pastoral Co. v. Gurney, 61 Fed. 41; Germania Iron Mining Co. v. King, 94 Wis. 439.

674 See Danbury & Norwalk R. Co. v. Wilson, 22 Conn. 435.

Where the call for payment of an assessment does not specify any time or place of payment, or the person to whom payment is to be made, it is payable on demand at the office of the corporation, and to any officer authorized to receive money due the corporation. Western Improvement Co. v. Des Moines Nat. Bank, 103 Iowa, 455.

675 Macon & Augusta R. Co. v. Vason, 57 Ga. 314; State Bank Building Co. v. Pierce, 92 Iowa, 668; Ogden Clay Co. v. Harvey, 9 Utah, 497.

Waiver as to one call or assessment is not a waiver as to subsequent ones. Somerset & Kenne-bec R. Co. v. Cushing, 45 Me. 524; quent ones. Atlantic De Laine Co. v. Mason, 5 R. I. 463.

676 York Tramways Co. v. Wil-38 Pa. St. 81; Danbury & Norwalk further assessment of thirty-five

R. Co. v. Wilson, 22 Conn. 435; Willamette Freighting Co. v. Stannus, 4 Or. 261; Wisconsin River Lumber Co. v. Walker, 48 Wis. 614; Kansas City Hotel Co. v. Harris. 51 Mo. 464.

A subscriber is estopped to object to a call on the ground that it was improperly made for the full amount of the subscriptions, where he participated as a director in making the call, and as a stockholder in instructing the directors to make the call. Stone v. Great Western Oil Co., 41 III. 85.

677 Philadelphia & West Chester R. Co. v. Hickman, 28 Pa. St. 318. And see Bavington v. Pittsburgh & Steubenville R. Co., 34 Pa. St. 358; Hays v. Pittsburgh & Steubenville R. Co., 38 Pa. St. 81.

678 Great Western Telegraph Co. v. Burnham, 79 Wis. 47, 24 Am. St. Rep. 698. In this case, the complaint in an action to recover an assessment on a subscription showed that some of the stockholders, including the defendant, had paid forty per cent. of their lows, 8 Q. B. Div. 685; Hays v. subscriptions, while others had Pittsburgh & Steubenville R. Co., paid but two per cent., and that a itself unequal, where the inequality is because of the fact that the favored stockholders have already paid more than the others, and the purpose is merely to render the contributions, as a whole, equal.679

(g) Partial invalidity.—The fact that one of several assessments is invalid does not render all of them invalid, but those which are invalid may be abandoned, and those which are valid enforced.680

#### § 500. Notice of calls and demand of payment.

By the weight of authority, in the absence of provision to the contrary in the charter, articles of association, by-laws, or contract of subscription, subscribers of stock are bound to take notice of all calls upon the subscriptions, and the directors are not required to give any notice, or to make any further demand of payment, before maintaining an action. 681 If, however, the

was unequal, partial, and invalid. See, also, Bowen v. Kuehn, 79 Wis. 53; Pike v. Bangor & Calais Shore Line R. Co., 68 Me. 445; Brockway v. Gadsden Mineral Land Co., 102 Ala. 620.

Co., 9 Heisk. (Tenn.) 545.

681 Smith v. Indiana & Illinois Ry. Co., 12 Ind. 61; Heaston v. Cincinnati & Ft. Wayne R. Co., 16 Ind. 275, 79 Am. Dec. 430; Lake Ontario, Auburn & N. Y. R. Co. v. Mason, 16 N. Y. 451; United Grow-Y.) 1; Eppes v. Mississippi, Gainesville & T. R. Co., 35 Ala. 33; Grubbs v. Vicksburg & Brunswick R. Co., 50 Ala. 398; Wilson v. Wills Valley R. Co., 33 Ga. 466; Swan v. Pittsburg Driving Park & Fair Ass'n, 6 Kan. App. 572.

unless otherwise expressly provid- given in some paper" of the time ed by law or the articles of incor- and place of paying any installporation, the directors of any cor- ment on subscriptions is complied

per cent. was levied upon all stock- poration may call in the subscripholders. A demurrer was sustain- tions to the capital stock by ined on the ground that the com-stallments by giving such notice plaint showed that the assessment thereof as the by-laws shall prescribe, to render a call enforceable, in the absence of any express provision of law, or of the articles of incorporation, fixing the time for its payment, a notice to be given must be prescribed by a by-law, or 679 Brockway v. Gadsden Mineral Land Co., 102 Ala. 620. ing the effect of a by-law. Gereso Read v. Memphis Gayoso Gas mania Iron Mining Co. v. King, 94 Wis. 439, 36 L. R. A. 551.

Under a statute authorizing the directors of a corporation to call in the subscriptions to its stock by giving such notice as may be prescribed by its by-laws, notice of a call by mailing a copy to subscribers Co. v. Eisner, 22 App. Div. (N. ers is insufficient, in the absence of a by-law authorizing notice in such manner, although the directors have made a resolution directing such notice. North Milwaukee Town Site Co. v. Bishop, 103 Wis. 492, 45 L. R. A. 174.

A statute requiring that "at Under a statute providing that, least sixty days' notice shall be charter, articles of association, by-laws, or subscription requires that a particular notice be given, or demand made, such notice or demand is necessary before an action can be maintained. 682 unless it is affirmatively shown that the subscriber had actual notice. A charter or statute or the articles of association may provide for publication of notice of calls in a newspaper, or in several newspapers, or in some other particular mode, and in such a case compliance with the requirement is generally necessary.683 When a particular notice is thus required no other or further notice is necessary.684

Proof of actual notice renders failure to give the notice required by the charter of the corporation harmless and immaterial 685

The notice need not be given in any particular mode, unless there is some express requirement. 686 But there must be reasonable notice. When notice is required, but publication of notice in a newspaper is not expressly authorized, such notice is not sufficient, unless actual notice is shown.687 Notice by mail is

with where a notice is published once only, if it is published sixty full days before the day of payment. Muskingum Valley Turnpike Co. v. Ward, 13 Ohio, 120, 42 Am. Dec. 191.

See, as to form of notice, San Joaquin Land & Water Co. v. Beech-

er, 101 Cal. 70.

682 Rutland & Burlington R. Co. v. Thrall, 35 Vt. 536; Dexter & Mason Plankroad Co. v. Millerd, 3 Mich. 91; Morris v. Metalline Land Co., 164 Pa. St. 326, 44 Am. St. Rep. 614; Banet v. Alton & Sanlution making the call, gamon R. Co., 13 III. 504; Spangler ered notices to other s. v. Indiana & Illinois Central Ry. Schenectady & Saratoga Co., 21 III. 276; Tomlin v. Tonica & Petersburg R. Co., 23 III. 429; Cole v. Joliet Opera House Co., 79

Cole v. Joliet Opera House Co., 79

Dangerfield, L. R. 3 Ill. 96; Hughes v. Antietam Mfg. Co., 34 Md. 316; Granite Roofing Co. v. Michael, 54 Md. 65; Macon & Augusta R. Co. v. Vason, 57 Ga. 314; Alabama & Florida R. Co. v. Rowley, 9 Fla. 508.

683 Morris v. Metalline Land Co., 164 Pa. St. 326, 44 Am. St. Rep. & S. (Pa.) 156, 37 Am. Dec. 500. 614.

684 Heaston v. Cincinnati & Ft. Wayne R. Co., 16 Ind. 275, 79 Am. Dec. 430; Germantown Passenger Ry. Co. v. Fitler, 60 Pa. St. 124, 100 Am. Dec. 546.

685 Jones v. Sisson, 6 Gray (Mass.) 288; Mississippi, Ouachita & R. R. R. Co. v. Gaster, 20 Ark. 455; Schenectady & Saratoga Plank Road Co. v. Thatcher, 11 N. Y. 102. Want of notice of calls, as re-

quired by statute, cannot be set up by a subscriber who, as a director of the company, voted for the resolution making the call, and delivered notices to other subscribers. Schenectady & Saratoga Plank Road

686 Shackleford, Ford & Co. v. Dangerfield, L. R. 3 C. P. 407; Smith v. Tallassee Branch of Central Plank-Road Co., 30 Ala. 650.

A notice of assessment is not rendered invalid by a mistake in the corporate name, if it is not such as to mislead. Gray v. Monongahela Navigation Co., 2 Watts 687 People's Building & Loan insufficient unless it is received. 688 Written notice is not necessary unless expressly required. 689

Where the charter of a corporation requires notice of calls to be given as prescribed by the by-laws, and such notice is given, no other notice or demand of payment is necessary. 690

VIII. ASSIGNMENT, MORTGAGE, OR PLEDGE OF UNPAID SUBSCRIPTIONS.

In general.—A corporation may sell, pledge, mortgage, or assign its unpaid stock subscriptions, if no call is necessary, or if a call, when necessary, has been made; but by the weight of authority, in the absence of an express grant of power, it cannot do so where a call is necessary, and has not been made.

When a corporation has a claim against a stockholder for an unpaid subscription to its capital stock, and no call is necessary to entitle it to payment, and to maintain an action thereon, or a call, if necessary, has been made, the claim is like any other chose in action constituting a part of its assets, and it may, for a legitimate corporate purpose, sell, pledge, mortgage, or assign the same in payment of a debt, or in trust for the benefit of creditors generally. 691 "A stock subscription is nothing but a contract, by which the subscriber is bound to pay the company certain amounts. It would clearly be assignable as between in-

9 Fla. 508.

Contra, Hall v. United States Ins. Co., 5 Gill (Md.) 484. 688 Hughes v. Antietam Mfg. Co., 34 Md. 316. See, also, Braddock v. Philadelphia, Marlton & M. R. Co., 45 N. J. Law, 363.

But it is sufficient if it is actually received. Elizabeth City Cotton Mills v. Dunstan, 121 N. C. 12,

61 Am. St. Rep. 654. 689 Smith v. Tallassee Branch of Central Plank-Road Co., 30 Ala.

690 Penobscot R. Co. v. Dummer,

Ass'n v. Furey, 47 N. J. Eq. 410; surance Society, L. R. 10 Eq. 312; Lake Ontario, Auburn & N. Y. R. In re Sankey Brook Coal Co., L. R. Co. v. Mason, 16 N. Y. 451; Ala- 9 Eq. 721, 10 Eq. 381; Wells v. bama & Florida R. Co. v. Rowley, Rodgers, 50 Mich. 294; Lewis' In re Sankey Brook Coal Co., L. R. 9 Eq. 721, 10 Eq. 381; Wells v. Rodgers, 50 Mich. 294; Lewis' Adm'r v. Glenn, 84 Va. 947; Morris v. Cheney, 51 III. 451; Miller v. Malony, 3 B. Mon. (Ky.) 105; Coler v. Grainger (C. C. A.) 74 Fed. 16; Shockley v. Fisher, 75 Mo. 498; Shultz v. Sutter, 3 Mo. App. 137; Franklin v. Menown, 11 Mo. App. 592: Roeppler v. Menown, 17 Mo. 592; Boeppler v. Menown, 17 Mo. App. 447; Downie v. Hoover, 12 Wis. 174, 78 Am. Dec. 730; Racine County Bank v. Ayres, 12 Wis. 512; Kimball v. Spicer, 12 Wis. 668; Rand v. Wiley, 70 Iowa, 110; Germantown Passenger Ry. Co. v. Fitler, 60 Pa. St. 124, 100 Am. Dec. 40 Me. 172, 63 Am. Dec. 654. 546; Chattanooga, Rome & cor In re International Life As- Co. v. Warthen, 98 Ga. 599. 546; Chattanooga, Rome & C. R. dividuals, and we can see no reason why it should not in the case of a corporation, acting in execution of the powers conferred by its charter."692 Whether or not unpaid subscriptions pass under a sale or other transfer of assets of a corporation depends, of course, upon the terms of the contract and the intention of the parties. 698 Unpaid subscriptions, if due, will pass with the other assets under a general assignment for the benefit of creditors, and may be collected by the assignee. 694

What has been said above applies only to subscriptions which are due, and for which no future call is necessary. By the weight of authority, in the absence of charter or statutory authority, a corporation cannot pledge, mortgage, or assign unpaid subscriptions when a call is necessary and has not been made. so as to entitle the pledgee, mortgagee, or assignee to collect the same, for in such a case the making of the call is discretionary with the directors or stockholders, and they cannot delegate the exercise of such discretion to another unless expressly authorized to do so.695

Of course, the charter of a corporation, articles of association, or general law may expressly authorize a corporation to pledge. mortgage, or assign its unpaid stock subscriptions, whether a call is necessary or not. 696 Whether such power is conferred or not depends upon the intent, and is a question of construction. It has been held that a general grant to a corporation of

174, 78 Am. Dec. 730.

693 The purchase by one railroad company of the road bed only of another, with intent to complete the road, gives it no right to purchase or enforce the latter's unpaid stock subscriptions. West-End Narrow-Gauge R. Co. v. Dameron, 4 Mo. App. 414.

Where a stockholder merely agrees to accept such drafts as the corporation shall draw on him for sales of stock, and the corporation makes a draft on him, and delivers it to another for value, this is not an assignment of the sum due from the stockholder to the corporation. Div. 534.

692 Downie v. Hoover, 12 Wis. Bank of Commerce v. Bogy, 9 Mo. App. 335.

694 See post, chapter xxv.

695 In re Joint Stock Cos., 4 De Gex, J. & S. 407; In re Sankey Brook Coal Co., L. R. 10 Eq. 381; Jackson v. Rainford Coal Co. (1896) 2 Ch. 340; Howard v. Patent Ivory Mfg. Co., 38 Ch. Div. 156; New Jersey Midland Ry. Co. v. Strait, 35 N. J. Law, 322; Shultz v. Sutter, 3 Mo. App. 137; Wells v. Rodgers, 50 Mich. 294. But see Lionberger v. Broadway Savings Bank, 10 Mo. App. 499; Eppright v. Nickerson, 78 Mo. 482. Nickerson, 78 Mo. 482.

696 See In re Pyle Works, 44 Ch.

the power to mortgage or pledge its "funds or property" does not confer the power to mortgage or pledge future assessments or calls upon unpaid subscriptions.697 It has also been held that a grant of power to sell unpaid subscriptions does not include the power to mortgage or pledge the same,698 but the better opinion is to the contrary. 699

### IX. INTEREST ON SUBSCRIPTIONS.

§ 502. In general.—A subscriber for stock is chargeable with interest on his subscription from the time he is in default, but not before, unless there is an express provision or stipulation to the

Sometimes a penalty is imposed for nonpayment of assessments.

The liability of a subscriber for interest on his subscription, in the absence of an express provision or stipulation, is the same as in the case of any other contract to pay money. Interest does not begin to run until he is in default, but, as soon as he is in default, it begins to run, and continues to run until payment. If no call is necessary, as explained in another section,700 interest runs from the time the subscription is due,from the date of the subscription, if it is payable immediately, or from the day fixed for payment, when it is payable on a certain day.701

If a subscription is payable upon call, interest runs from the date of the call, or from the time of payment fixed by the call, when no notice or demand is required. 702 If notice is required, interest runs from the time of notice, and not be-

Gex, J. & S. 407, and other cases in the preceding note.

<sup>698</sup> Morris v. Cheney, 51 III. 451. 699 In re International Life Assurance Society, L. R. 10 Eq. 312; In re Sankey Brook Coal Co., L. R.

<sup>697</sup> In re Joint Stock Cos., 4 De App. 618; Rikhoff v. Brown's Rotary Shuttle Sewing-Machine Co., 68 Ind. 388. But see Frank v. Morrison, 55 Md. 399.

When subscriptions are payable in monthly installments, without demand, each installment bears in-10 Eq. 381.

10 Eq. 381.

10 Ante, § 498.

10 In terest from the time it becomes due. Hawkins v. Citizens' Real Estation of Oneonta, 71 N. Y. 298;

Town of Oneonta, 71 N. Y. 298;

Seattle Trust Co. v. Pit-

fore. 703 Where a call is made by an order or decree of a court, or by an authorized order of a public officer, as by the comptroller of the currency in the case of an insolvent national bank. interest runs from the date of the order.704

Sometimes a statute imposes a specific penalty upon subscribers for nonpayment of assessments upon their stock, to be recovered in an action by the corporation. Where a statute authorized a corporation to charge five per cent. interest per month on all stock subscribed, if not paid within thirty days, it was held that this was not interest, but a penalty.705

X. Subscription of Full Amount of Capital Stock, or of a Speci-FIED PERCENTAGE THEREOF.

§ 503. In general.—Subscription of the full amount of the authorized capital stock of a corporation is sometimes made a condition precedent to incorporation, or to the right to commence business; but it is not so unless it is expressly so provided.

A subscription to the stock of a corporation may, in express terms, make the subscription of the full amount, or a certain percentage, of the capital stock a condition precedent to liability thereon. And such a condition is often implied. It is a general rule that, in the absence of anything to show a contrary intention, every subscription is upon the implied condition that the full amount of the capital stock fixed by the charter, enabling act, articles of association, or contract of subscription, or by the act of the directors or stockholders when they are authorized to settle the same, shall be subscribed in good faith before the subscriber is called upon to pay anything on his subscription. In determining the amount of stock subscribed, only bona fide, absolute, and binding subscriptions can be counted.

ner, 18 Wash. 401; McCoy v. poration. Seattle Trust Co. v. Pit-World's Columbian Exposition, 87 ner, 18 Wash. 401. Ill. App. 605, 186 Ill. 356, 78 Am. St. Rep. 288; Jackson Fire & Marine Ins. Co. v. Walle, 105 La. 89.

It has been held that interest is not payable on a note given for a subscription to stock, although payno call for payment of subscrip- 70; Bavington v. Pittsburgh & tions has been made by the cor- Steubenville R. Co., 34 Pa. St. 358.

703 Hambleton v. Glenn, 72 Md. 331; American Pastoral Co. v. Gurney, 61 Fed. 41.

704 Casey v. Galli, 94 U. S. 673. 705 Custar v. Titusville Gas & Water Co., 63 Pa. St. 381. As to ment is not made until after the the construction of such statutes, date named in the note, if there is see Delaware & Schuylkill Canal no agreement to pay interest, and Navigation v. Sansom, 1 Bin. (Pa.)

This rule does not apply where it appears from the charter, enabling act, articles of association, or contract of subscription that subscription of the full amount of the capital stock was not intended as a condition precedent to liability. Nor does it apply where the condition is waived by the subscriber, or he is estopped by his conduct from setting up its nonperformance.

### § 504. As a condition precedent to legal incorporation or transaction of business.

The charter or enabling act under which a corporation is organized sometimes requires that the full amount of its capital stock, or a certain percentage thereof, shall be subscribed as a condition precedent to incorporation, and in such a case legal existence as a corporation cannot be acquired until the condition is performed. 706 But subscription of the whole or any particular part of the capital stock is not a condition precedent to acquiring a corporate existence, unless it is made so by the charter or statute.707

Subscription for the full amount of stock, or a certain percentage thereof, may also be made a condition precedent to the right to commence business and contract debts,708 and the

Central Plank-Road Co., 30 Ala. Y. 102; Smock v. Henderson, 1 650; People v. Chambers, 42 Cal. Wils. (Ind.) 241; McGinty v. 201; Wellersburg & West Newton Athol Reservoir Co., 155 Mass. 183; Plank Road Co. v. Hoffman, 9 Md. Perkins v. Sanders, 56 Miss. 733; 559; Garrett v. Dillsburg & Mechanicsburg R. Co., 78 Pa. St. 465; National Bank of Jefferson v. Attorney General v. Chicago & Texas Investment Co., 74 Tex. 421; Northwestern Ry. Co., 35 Wis. 425; Hammond v. Straus, 53 Md. 1. Anderson v. Newcastle & Richmond R. Co., 12 Ind. 376, 74 Am. Dec. 218; Jersey City Gas Co. v. Dwight, 29 N. J. Eq. 246; Livesey v. Omaha Hotel, 5 Neb. 50; Leighty v. Susquehanna & Waterford Turnpike Co., 14 Serg. & R. (Pa.) 434; Boyd v. Peach Bottom Ry. Co., 90

706 Smith v. Tallassee Branch of Plank Road Co. v. Thatcher, 11 N.

708 Trammell v. Pennington, 45 Ala. 673; Academy of Music v. Flanders, 75 Ga. 14; Burns v. Beck & Gregg Hardware Co., 83 Ga. 471; Livesey v. Omaha Hotel, 5 Neb. 50; Spartanburg & Asheville R. Co. v. Ezell, 14 S. C. 281.

But it is not so unless it is so Pa. St. 169; Lake Ontario, Auburn provided. Newcastle & Anderson-& N. Y. R. Co. v. Mason, 16 N. Y. town Turnpike Co. v. Bell, 8 Blackf. 451. (Ind.) 584; Johnson v. Kessler, 76
707 Minor v. Mechanics' Bank, 1 Iowa, 411; Hunt v. Kansas & MisPet. (U. S.) 46; Willamette souri Bridge Co., 11 Kan. 412; MasFreighting Co. v. Stannus, 4 Or. sey v. Citizens' Building & Sav261; Schenectady & Saratoga ings Ass'n, 22 Kan. 624. stockholders may be made liable individually for debts contracted in violation of the prohibition, 709

Where charter or statutory requirements of subscriptions to a certain amount are not conditions precedent to incorporation. but conditions subsequent, 710 noncompliance therewith, while it may render the charter of the corporation subject to forfeiture in proceedings by the state,711 will not affect the existence of the corporation before such proceedings are instituted, and a forfeiture adjudged. The organization and legal existence of a railroad corporation are not affected by noncompliance with a requirement in its charter that a certain percentage of the cost shall be subscribed before it shall commence the construction of any section of its road.713

### § 505. As a condition precedent to enforcement of subscriptions.

Subscriptions for stock in corporations are sometimes made in terms upon the express condition that the full amount of the capital stock of the corporation, or a specified percentage thereof, shall be subscribed, or shall be subscribed by certain persons, or persons of a certain class; and in such a case, they cannot be enforced by the corporation, in the absence of a waiver or an

709 See Wechselberg v. Flour City Nat. Bank, 24 U. S. App. 308, 64 Fed. 90; Chase's Patent Elevator Co. v. Boston Tow-Boat Co., 152

710 See ante, §§ 73, 313(b).

711 People v. National Savings Bank, 11 N. E. 170; affirmed 129 Ill. 618; Holman v. State, 105 Ind. 569.

Where the charter of a corporation authorizes it to commence business only when one thousand shares of its stock have been subscribed, commencement of business when only a few hundred shares have been subscribed is ground for proceedings to forfeit its charter. State v. Debenture Guarantee & Loan Co., 51 La. Ann. 1874.

712 Stokes v. Findlay, 4 McCrary, 205, Fed. Cas. No. 13,478; Young Me. 512, 66 Am. Dec. 257.

Reversible Lock-Nut Co. v. Young Lock-Nut Co., 72 Fed. 62; Smith v. Tallassee Branch of Central Plank-Road Co., 30 Ala. 650; Hammond v. Straus, 53 Md. 1.

But where an act incorporating a banking company provided that there should be a certain amount of capital stock, that no increase should be made unless the amount thereof should be paid in, that, before commencement of business, the stockholders should pay their subscriptions in full, and that the act should become void unless the corporation should organize and proceed to business within two years, it was held that failure to subscribe and pay in the capital stock within two years forfeited the charter. People v. National Savings Bank, 129 Ill. 618.

713 Penobscot R. Co. v. White, 41

estoppel, until the condition has been substantially performed or fulfilled.714

Such a condition may also be implied, when not expressed. As a general rule, every person who becomes a subscriber for original stock in a corporation has a right to assume that the full amount of the capital stock fixed by the charter or enabling act, or by the articles of association or the contract of subscription, or by the directors or stockholders when they are authorized to settle the same, will be subscribed in good faith and unconditionally, before he is called upon to pay anything on his subscription; and therefore, in the absence of anything to show a contrary intention on the part of the legislature or the subscribers, every subscription is upon the condition, implied when

714 Cravens v. Eagle Cotton Mills Co., 120 Ind. 6, 16 Am. St. Rep. 298; Shick v. Citizens' Enterprise Co., 15 Ind. App. 329; Union Hotel Co. v. Hersee, 79 N. Y. 454, 35 Am. Rep. 536; New York Exchange Co. v. De Wolf, 31 N. Y. 273; Brand v. Lawrenceville Branch R. Co., 77 Ga. 506; Branch v. Augusta Glass Works, 95 Ga. 573; Phillips v. Covington & Cincinnati Bridge Co., 2 Metc. (Ky.) 210; Philadelphia & West Chester R. Co. v. Hinchman, 28 Pa. St. 318; Porter v. Raymond, 53 N. H. 519; People's Ferry Co. v. Balch, 8 Gray (Mass.) 303; Troy & Greenfield R. Co. v. Newton, 8 Gray (Mass.) 596; Santa Cruz R. Co. v. Schwartz, 53 Cal. 106; Monadnock Railroad v. Felt, 52 N. H. 379; Hahn's Appeal (Pa.) 7 Atl. 482: Monthelier & Walls Biver B. 482; Montpelier & Wells River R. Co. v. Langdon, 45 Vt. 137; Johnson v. Schar, 9 S. D. 536.

A person who is engaged in business in a certain city, and spends nearly all of his time there, but who has his legal domicile in another city, is a citizen of the former city, within the meaning of a condition in a subscription for stock in a hotel company that a certain amount of stock shall be city. Union Hotel Co. v. Hersee. subscribed. Hickling v. Wilson, 79 N. Y. 454, 35 Am. Rep. 536.

A contract of subscription upon condition that a certain amount of stock shall be subscribed by others may be modified, by agreement between the subscriber and the corporation, by reducing the amount to be subscribed by others. Emmitt v. Springfield, Jackson & P. R. Co., 31 Ohio St. 23.

A condition in a subscription that 500 shares shall be taken "under the terms hereof" is not performed by the taking of subscriptions aggregating 500 shares, some of which are under different terms. Johnson v. Schar, 9 S. D. 536.

A condition in a subscription for stock that a certain amount of stock shall be subscribed for "by" a certain day is fulfilled if the total subscriptions reach that amount on the night of that day, for the word "by," when used to designate a terminal point of time, means "not later than" Elizabeth City "not later than." Elizabeth City Cotton Mills v. Dunstan, 121 N. C. 12, 61 Am. St. Rep. 654.

If subscriptions are absolute and unconditional on their face, they cannot be qualified or limited by proof of a general understanding among the subscribers that they were not to be collected unless a subscribed by the citizens of such given amount of stock should be not expressed, that there shall be no liability thereon until the full capital stock or the required percentage thereof has been in good faith subscribed for.<sup>715</sup> This rule applies whether the

715 United States: Winters v. Armstrong, 37 Fed. 508.

California: Santa Cruz R. Co. v. Schwartz, 53 Cal. 106; San Bernardino Investment Co. v. Merrill, 108 Cal. 490; Ventura & Ojai Valley Ry. Co. v. Hartman, 116 Cal. 260.

Colorado: Stearns v. Sopris, 4

Colo. App. 191.

Connecticut: New York, Housatonic & N. R. Co. v. Hunt, 39 Conn. 75.

Georgia: Brand v. Lawrenceville Branch R. Co., 77 Ga. 506; Hendrix v. Academy of Music, 73 Ga. 437; Memphis Branch R. Co. v. Sullivan, 57 Ga. 240.

Illinois: Temple v. Lemon, 112 Ill. 51; Allman v. Havana, Rantoul & E. R. Co., 88 Ill. 521.

Indiana: Hain v. North Western Gravel Road Co., 41 Ind. 196; Fox v. Allensville, C. S. & V. Turnpike Co., 46 Ind. 31.

Iowa: Peoria & Rock Island R. Co. v. Preston, 35 Iowa, 115.

Kansas: Topeka Bridge Co. - Cummings, 3 Kan. 55.

Kentucky: Fry's Ex'r v. Lexington & Big Sandy R. Co., 2 Metc.

(Ky.) 314.

Louisiana: State v. Atchafalaya Railroad & Banking Co., 5 Rob. (La.) 63; Exposition Railway & Improvement Co. v. Canal Street Exposition Ry. Co., 42 La. Ann. 370.

Maine: Penobscot R. Co. v. Dummer, 40 Me. 172, 63 Am. Dec. 654; Penobscot R. Co. v. White, 41 Me. 512, 66 Am. Dec. 257; Lewey's Island R. Co. v. Bolton, 48 Me. 451, 77 Am. Dec. 236; Rockland, Mt. Desert & S. Steamboat Co. v. Sewall, 78 Me. 167, 80 Me. 400; Oldtown & Lincoln R. Co. v. Veazie, 39 Me. 571.

Maryland: Hughes v. Antietam Mfg. Co., 34 Md. 316; Baile v. Calvert College Educational Society, 47 Md. 117.

Massachusetts: Salem Mill Dam Corp. v. Ropes, 6 Pick. (Mass.) 23, 2 Keener's Cas. 1245; Id., 9 Pick. (Mass.) 187, 19 Am. Dec. 363; Atlantic Cotton Mills v. Abbott, 9 Cush. (Mass.) 423; Cabot & West Springfield Bridge v. Chapin, 6 Cush. (Mass.) 50; Stoneham Branch R. Co. v. Gould, 2 Gray (Mass.) 277; People's Ferry Co. v. Balch, 8 Gray (Mass.) 303; Troy & Greenfield R. Co. v. Newton, 8 Gray (Mass.) 596.

Michigan: International Fair & Exposition Ass'n v. Walker, 88 Mich. 62; Shurtz v. Schoolcraft & Three Rivers R. Co., 9 Mich. 270; Monroe v. Ft. Wayne, Jackson & S. R. Co., 28 Mich. 272; Halsey Fire-Engine Co. v. Donovan, 57 Mich. 318; Curry Hotel Co. v. Mullins, 93 Mich. 318; Swartout v. Michigan Air Line R. Co., 24 Mich.

389.

Minnesota: Masonic Temple Ass'n v. Channell, 43 Minn. 353.

Mississippi: Selma, Marion & M. R. Co. v. Anderson, 51 Miss. 829.

Missouri: Haskell v. Worthington, 94 Mo. 560; Sedalia, Warsaw & S. Ry. Co. v. Abell, 17 Mo. App. 645.

Nebraska: Livesey v. Omaha Hotel. 5 Neb. 50; Hale v. Sanborn, 16 Neb. 1; Estabrook v. Omaha Hotel, 5 Neb. 76; Hards v. Platte Valley Improvement Co., 35 Neb. 263.

New Hampshire: New Hampshire Central R. Co. v. Johnson, 30 N. H. 390, 64 Am. Dec. 300; Little ton Mfg. Co. v. Parker, 14 N. H. 543; Contoocook Valley R. Co. v. Barker, 32 N. H. 363.

New York: Union Hotel Co. v. Hersee, 79 N. Y. 454, 35 Am. Rep. 536; Bray v. Farwell, 81 N. Y. 600.

Oregon: Portland & Fairview R. Co. v. Spillman, 23 Or. 587.

Pennsylvania: Philadelphia & West Chester R. Co. v. Hickman, 28 Pa. St. 318; Spellier Electric

amount of the capital stock is fixed by the charter or enabling act, or by the articles of association in pursuance thereof, or by a resolution of the stockholders or directors, when they are authorized to settle the same, or by the contract of subscription itself. The When the liability on subscriptions is thus conditional upon the subscription of the full amount or a certain percentage of the capital stock, and there is no waiver of the condition, an assessment or call before the condition is performed is in-And it is none the less invalid because the condition valid.717 is performed on the same day, but after dissolution of the meeting of the directors at which the assessment or call was made. 718 The rule, however, does not prevent the levy of a sufficient assessment to defray necessary and contemplated preliminary expenses.<sup>719</sup> And as we shall see in a subsequent section, a subscriber may waive the condition or be estopped to set up its nonperformance.720

When the condition is not implied.—The general rule that subscriptions are upon the implied condition that the full amount of the capital stock shall be subscribed does not apply where a contrary intention appears from the provisions of the charter or enabling act, or, unless it is required by the charter or en-

Time Co. v. Leedom, 149 Pa. St.

Rhode Island: Warwick R. Co. v. Cady, 11 R. I. 131.

Tennessee: Read v. Memphis Gayoso Gas Co., 9 Heisk. (Tenn.) 545; Anderson v. Middle & East Tennessee Central R. Co., 91 Tenn.

Texas: Galveston Hotel Co. v. Bolton, 46 Tex. 633; Orynski v. Loustaunan (Tex.) 15 S. W. 674.

Connecticut & Pas-Vermont: sumpsic Rivers R. Co. v. Bailey, 24 Vt. 465, 58 Am. Dec. 181.

Virginia: Norwich Lock Mfg.

Co. v. Hockaday, 89 Va. 557.
Washington: Denny Hotel Co.
v. Schram, 6 Wash. 134, 36 Am.
St. Rep. 130; Birge v. Browning, 11 Wash, 249.

Wisconsin: Anvil Mining Co. v. Sherman, 74 Wis. 226.

716 See the cases in the note preceding.

"It is well settled that there is an implied condition that the amount of stock specified in the charter, articles of association, or contract of subscription, or fixed by the corporators when authorized to settle same, shall be actually taken before the subscribers shall become liable." Anderson v. Middle & East Tennessee Central R. Co., 91 Tenn. 44.

717 See the cases above cited.

718 Stoneham Branch R. Co. v. Gould, 2 Gray (Mass.) 277.

719 Salem Mill Dam Corp. v. Ropes, 6 Pick. (Mass.) 23, 2 Keener's Cas. 1245; Id., 9 Pick. (Mass.) 187, 19 Am. Dec. 363; Anvil Mining Co. v. Sherman, 74 Wis. 226.

720 Post, § 507.

abling act as a condition precedent to corporate existence, where a contrary intention appears from the provisions of the articles of association, or by the action of the stockholders or directors fixing the capital stock, or by the terms of the contracts of subscription.<sup>721</sup> If it appears therefrom, by express terms or clear implication, that it was intended that the corporation should or might engage in business before subscription of the full amount of its capital stock, or make contracts, create debts, or do any other act involving a necessity to call upon stockholders to pay their subscriptions, it cannot be implied that it was intended to make the subscription of the whole amount of the capital stock a condition precedent to liability on subscriptions, and it will not be so held.722

It has been held, for example, that there is no such implied condition where the articles of association provide that the "capital stock of the said corporation shall be fifty thousand dollars, of which fourteen thousand five hundred have been suband the residue may be issued and disposed scribed. of as the board of directors may from time to time order and direct;"723 or where the enabling act provides that "the regis-

Trimble, 54 Ark. 316; South Georgia & Florida R. Co. v. Ayres, 56 Ga., 230; Penobscot & Kennebec R. Co. v. Bartlett, 12 Gray (Mass.)
244, 71 Am. Dec. 753; Boston & Washington Plank Road Co. v. Barre & G. R. Co. v. Wellington, 113 Mass. 79; Kennebec & Portland R. Co. v. Jarvis, 34 Me. 360; Bucksport & Bangor R. Co. v. Mortgomery Trade Co., 87 Ala. Hill, 13 Am. St. Rep. 51; Musgrave Bucksport & Bangor R. Co. v. Morrison, 54 Md. 161; Perkins Buck, 65 Me. 536; Skowhegan & Athens R. Co. v. Kinsman, 77 Me. Crawford, 80 Cal. 19; Auburn 370; Mandel v. Swan Land & Cattle Co., 154 Ill. 177, 45 Am. St. Rep. 111. (Cal.) 32 Pac. 587; Belton 124, reversing 51 Ill. App. 204; Compress Co. v. Saunders, 70 Tex. Hoagland v. Cincinnati & Ft. 699; Cheraw & Chester R. Co. v. Wannesota R. Co. v. Perkins, 25 Lowa, 281; Lincoln Shoe Mfg. Co. v. Sheldon, 44 Neb. 279; Warwick R. Co. v. Cady, 11 R. I. 131; Lynch Saratoga Plank Road Co. v. Thatcher, 11 N. Y. 102; Rensselaer Thatcher, 11 N. Y. 102; Renss 56 Ga., 230; Penobscot & Kennebec

721 Anderson v. Middle & East v. Eastern, La Fayette & M. Ry. Tennessee Central R. Co., 91 1 cm.,
44; Cheraw & Chester R. Co. v. Centralia & N. Ry. Co. v. Arpin, C. Garland, 14 S. C. 63; and cases in the notes following.

34 Ohio St. 601; Astoria & South Coast R. Co. v. Hill, 20 Or. 177; Stannus, 4 Or. 261; Schenectady & Saratoga Plank Road Co. v. Thatcher, 11 N. Y. 102; Rensselaer & Washington Plank Road Co. v.

tered holders of shares in the company, for the time being, whatever the number issued or subscribed for," shall form the company, "and the business of the company may be commenced as soon as the directors think fit;"724 or where the charter of a corporation provides merely that its capital stock shall not exceed a certain amount, and the contracts of subscription bind the subscribers severally to pay the amount of their subscriptions in such manner as the directors may, under the charter, direct; 725 or where the corporation is engaged in its business at the time a subscription is made, and the subscriber knows that the full amount of its capital stock has not been subscribed. 726

If the charter of a corporation or the enabling act authorizes it to incorporate and commence business when a certain percentage of its capital is subscribed, it is not necessary that the full amount of its authorized capital stock shall be subscribed

may be inferred that the subscrip-tion was not upon condition that corporation "in such manner as the whole capital stock should be the by-laws might prescribe," did

Where the charter of a railroad company provided that its capital stock should be not less than 4,000 shares, nor more than 10,000 shares, and authorized it to organize when 4,000 shares should be subscribed, but provided that no contract for building its road should be made until subscription of 7,000 shares, it was held that the liability of subscribers attached when 4,000 shares were subscribed, and the corporation was organized and though no vote was passed fixing capital stock is a condition preced-the amount of the stock, and the ent to liability on subscriptions, 10,000 shares had not been taken. Penobscot & Kennebec R. Co. v. Bartlett, 12 Gray (Mass.) 244, 71 Am. Dec. 753.

728 Arkadelphia Cotton Mills v. Trimble, 54 Ark. 316.

In a Texas case, however, it was Md. 161. As to waiver, see post. § held that a statute conferring upon 507.

tion is already engaged in busi- the directors the general manageness, and that the whole capital ment of a corporation, and empowstock has not been subscribed, it ering them to dispose of the unsubscribed. Musgrave v. Morrison, not, in the absence of any by-laws 54 Md. 161. on the subject, authorize them to enforce an unpaid subscription before all the capital stock was taken. Orynski v. Loustaunan (Tex.) 15 S. W. 674.

724 Mandel v. Swan Land & Cattle Co., 154 Ill. 177, 45 Am. St. Rep. 124, reversing 51 Ill. App. 204.

A statute which merely provides that, when articles of incorporation are filed and published according to law, the incorporators are authorized to carry into effect the objects of the corporation, does passed a vote to dispose of the not abrogate the common-law rule rest of the stock authorized, al- that the subscription of the full in the absence of anything to show a contrary intent. Masonic Temple Ass'n v. Channell, 43 Minn. 353. 725 Warwick R. Co. v. Cady, 11

> R. I. 131. 726 Musgrave v. Morrison, 54

before calling for payment on subscriptions, but it is necessary that the required percentage shall be subscribed.<sup>727</sup>

Increase of capital stock.—It has been held in a Tennessee case that the principle that the whole amount of capital stock fixed by the charter of a corporation must be subscribed before a valid assessment can be made upon subscriptions applies when an increase of capital stock is made under authority from the legislature. 728 By the weight of authority, however, this is not the rule unless full subscription is expressly required. An original stockholder who signs, without qualification, a subscription for new stock, to increase the original stock, is not entitled to cancellation of his subscription, and repayment of the amount paid in, on the ground that all the new shares have not been subscribed for. In the absence of any stipulation or limitation to the contrary, his subscription is not dependent upon the taking of all the shares, but is absolute.<sup>729</sup> Where a railroad company voted to issue six hundred additional shares, and to allow each stockholder to take one new share for every two shares already held by him, provided he should by a certain day subscribe therefor, and pay a part of the price, and give notes for the remainder, it was held that there was no implied condition that the whole number of six hundred new shares should be issued; and that the failure of the corporation to issue that num-

727 Hamilton & Deansville Plank Road Co. v. Rice, 7 Barb. (N. Y.) 157; Schenectady & Saratoga Plank Road Co. v. Thatcher, 11 N. Y. 102; Iowa & Minnesota R. Co. v. Perkins, 28 Iowa, 281; Schloss v. Montgomery Trade Co., 87 Ala. 411, 13 Am. St. Rep. 51; Boston, Barre & G. R. Co. v. Wellington, 113 Mass. 79; Bucksport & Bangor R. Co. v. Buck, 65 Me. 536; Jewett v. Valley Ry. Co., 34 Ohio St. 601; San Bernardino Investment Co. v. Merrill, 108 Cal. 490; Ventura & Ojai Valley Ry. Co. v. Hartman, 116 Cal. 260; Willamette Freighting Co. v. Stannus, 4 Or. 261; Astoria & South Coast R. Co. v. Hill, 20 Or. 177; State v. Atchafalaya Railroad & Banking Co., 5 Rob. (La.) 63.

The fact that a corporation is authorized to organize when less than the full amount of its capital stock is subscribed does not authorize it to commence business before subscription of the full amount, so as to permit it to enforce subscriptions before the full amount has been subscribed. Galveston Hotel Co. v. Bolton, 46 Tex. 633; Peoria & Rock Island R. Co. v. Preston, 35 Iowa, 115.

<sup>728</sup> Read v. Memphis Gayoso Gas Co., 9 Heisk. (Tenn.) 545.

<sup>720</sup> Avegno v. Citizens' Bank, 40 La. Ann. 799; Clarke v. Thomas, 34 Ohio St. 46; Greenbrier Industrial Exposition v. Ocheltree, 44 W. Va. 626 ber was no ground for an action by a stockholder to recover back money paid by him for the new stock, or for defeating an action on the notes given by him.<sup>730</sup>

Of course, a subscription for increased stock may be made conditional upon subscription of the full amount, either by the express terms of the statute authorizing the increase, or by the vote making the increase, or by the contract of subscription itself.731

## § 506. What subscriptions or promises may be counted.

In determining whether the entire capital stock of a corporation or a required percentage thereof has been subscribed, only bona fide, valid, and absolute subscriptions can be taken into consideration.

A guaranty by a person that subscriptions shall be made to the amount required by an express or implied condition is not equivalent to the subscriptions, and cannot be considered in determining whether the condition has been fulfilled. 732

Where a subscription is made upon condition that a certain amount of stock shall be subscribed, the amount of such subscription is to be counted in determining whether the condition has been performed, unless there is something to show a contrary intent.733

Fictitious subscriptions, and subscriptions by persons under legal disability.—Subscriptions in the names of fictitious persons clearly cannot be counted. 734 Nor is it permissible to count unpaid subscriptions by infants, which are voidable at their option:735 or by married women, where the disability arising from coverture has not been removed by statute, for at common

<sup>782</sup> Branch v. Augusta Glass Works, 95 Ga. 573.

<sup>738</sup> Montpelier & Wells River R. Co. v. Langdon, 45 Vt. 137.

<sup>730</sup> Nutter v. Lexington & West
Cambridge R. Co., 6 Gray (Mass.)
85.
781 Hahn's Appeal (Pa.) 7 Atl.
782 See Jersey City Gas Co. v.
Dwight, 29 N. J. Eq. 242; Lewey's
Island R. Co. v. Bolton, 48 Me. 451,
783 Hahn's Appeal (Pa.) 7 Atl.
784 See Jersey City Gas Co. v.
Dwight, 29 N. J. Eq. 242; Lewey's
Island R. Co. v. Bolton, 48 Me. 451,
785 Hahn's Appeal (Pa.) 7 Atl.
786 Hahn's Appeal (Pa.) 7 Atl.
787 Am. Dec. 236, and the cases
Research to the control of t

<sup>785</sup> Phillips v. Covington & Cincinnati Bridge Co., 2 Metc. (Ky.) 219; Hahn's Appeal (Pa.) 7 Atl. 482.

law such a contract by a married woman is void;<sup>736</sup> or by insane persons.737

Subscriptions by the corporation itself or by other corporations.

—A subscription by another corporation, where its charter does not expressly or impliedly authorize it to subscribe, cannot be counted in those jurisdictions in which such a contract, because ultra vires, is regarded as absolutely void and unenforceable; 738 but it is otherwise in those jurisdictions in which it is held that the subscribing corporation cannot set up its want of power to defeat an action on the subscription. The defense of ultra vires, and the conflicting doctrines in the different states, are considered at length in a former chapter. 740

A corporation cannot subscribe for shares of its own stock. either directly or through a trustee, and, if it does so, its subscription cannot be counted in determining the amount of stock subscribed. But one who subscribes as trustee for the corporation may be personally liable, and in such a case the subscription may be counted.\*

Subscriptions by insolvent or irresponsible persons.—Whether subscriptions by insolvent or irresponsible persons can be taken

786 Phillips v. Covington & Cincinnati Bridge Co., 2 Metc. (Ky.) 219; Hahn's Appeal (Pa.) 7 Atl.

Shares of stock issued to and in the name of a married woman, who receipted therefor at the instance of her husband, the husband paying assessments thereon, so as to render him personally liable for corporate debts, was held not to be the corporations, to bring the total stock issued to a married woman in such a sense as to be equivalent to its not having been subscribed for, so as to exclude it from the in determining reckoning subscribed. of stock amount Kampmann v. Tarver (Tex. Civ. App.) 29 S. W. 1144.

737 See the cases above cited. 738 Berry v. Yates. 24 Barb. (N. 367. Y.) 199; Denny Hotel Co. v. 740 Ante, § 204 et Schram, 6 Wash. 134, 36 Am. St. \*Johnston v. Allie Rep. 130; Denny Hotel Co. v. Gil- See ante, § 448(d).

more, 6 Wash. 152. See ante, §§ 193 et seq., 448(d).

The fact that some subscriptions were by corporations not authorized to subscribe is no defense in an action against persons who afterwards subscribed, where their subscriptions were sufficient, without counting the subscriptions by up to amount required. Walter A. Wood Harvester Co. v. Jefferson, 71 Minn. 367.

739 United States Vinegar Co. v. Foehrenbach, 148 N. Y. 58; McCoy v. World's Columbian Exposition, 87 Ill. App. 605, 186 Ill. 356, 78 Am. St. Rep. 288; Walter A. Wood Harvester Co. v. Jefferson, 71 Minn.

740 Ante, § 204 et seq. \*Johnston v. Allis, 71 Conn. 207.

into consideration depends upon the circumstances. If they were not made and accepted in good faith, but with knowledge that the subscribers were insolvent and irresponsible, they cannot be counted.741 But it is otherwise if they were made by persons apparently solvent and able to pay, and accepted in good faith, although it may appear that the subscribers were and still are totally insolvent.742

Conditional subscriptions.—Subscriptions upon conditions precedent cannot be counted in determining the amount of stock subscribed, even when they are valid, for such a subscription, as we have seen,743 imposes no liability upon the subscriber unless the conditions are performed or waived. 744 Subscriptions upon conditions precedent may be counted, however, if it affirmatively appears that the conditions have been performed, for they are then absolute and unconditional.745

219; Lewey's Island R. Co. v. Bolton, 48 Me. 451, 77 Am. Dec. 236; Belfast & Moosehead Lake R. Co. v. Inhabitants of Brooks, 60 Me. 568; Denny Hotel Co. v. Schram, 6 Wash. 134, 138, 36 Am. St. Rep. 130, 133.

742 Penobscot R. Co. v. Dummer, 40 Me. 172, 63 Am. Dec. 654; Penobscot R. Co. v. White, 41 Me. 512, 66 Am. Dec. 257; Belfast & Moosehead Lake R. Co. v. Inhabitants of Brooks, 60 Me. 568; Salem Mill Dam Corp. v. Ropes, 9 Pick. (Mass.) 187, 19 Am. Dec. 363; Litchfield Bank v. Church, 29 Conn. 137.

Declarations of a subscriber showing that his subscription was not made or accepted in good faith, but was fraudulent, made long after the organization of the corporation, are not admissible to affect the organization of the corporation, or the liability of other subscribers. Penobscot R. Co. v. White, 41

741 Phillips v. Covington & Cin-prietors of Cabot & West Spring-cinnati Bridge Co., 2 Metc. (Ky.) field Bridge v. Chapin, 6 Cush. field Bridge v. Chapin, 6 Cush. (Mass.) 50; People's Ferry Co. v. Balch, 8 Gray (Mass.) 303; New York Exchange Co. v. De Wolf, 31 N. Y. 273; Union Hotel Co. v. Hersee, 79 N. Y. 454, 35 Am. Rep. 536; New York, Housatonic & N. R. Co. v. Hunt, 39 Conn. 75; Portland & Fairview R. Co. v. Spillman, 23 Or. 587; Oskaloosa Agricultural Works v. Parkhurst, 54 Iowa, 357; Brand v. Lawrenceville Branch R. Co., 75 Ga. 506; Philadelphia & West Chester R. Co. v. Hickman, 28 Pa. St. 318; California Southern Hotel Co. v. Russell, 88 Cal. 277.

Where the statute under which a corporation was formed required articles of incorporation to be filed and a charter obtained before any subscriptions for stock, and one-half of the authorized capital stock to be subscribed before organization, it was held that a person might subscribe conditionally, and that the conditions would not be held void, and the subscription Me. 512, 66 Am. Dec. 257.

743 Ante, § 455 et seq.

744 Central Turnpike Corp. v. of stock had been subscribed.

Valentine, 10 Pick. (Mass.) 142;

Troy & Greenfield R. Co. v. Newton, 8 Gray (Mass.) 596; Pro
745 See the cases above cited.

As we have seen, conditional subscriptions cannot be received prior to incorporation. In New York it is held that such subscriptions are absolutely void, and therefore they cannot be counted in determining the amount of stock subscribed.746 Pennsylvania, on the other hand, it is held that such subscriptions are not void, but that the condition is void, and they may therefore be counted as absolute subscriptions.747

Subscriptions upon special terms.—Whether or not it is permissible to take into consideration subscriptions upon special terms. as distinguished from conditional subscriptions, 748 in determining the amount of stock subscribed, depends upon the nature and effect of the special terms. If they are valid, and reduce the amount payable on the subscription below the par value of the stock, it seems clear that they cannot be counted. 749 otherwise, however, if the full par value of the stock is payable without deduction, the special term being such as not to affect the amount to be paid. 750 A stipulation on the part of a railroad corporation to pay interest on the sums paid in by subscribers until the construction of its road is no ground for not counting the subscriptions.751 According to the weight of authority, subscriptions payable in property, labor, or services, or construction work, although at a fair valuation, cannot be count $ed.^{752}$ 

Of course, subscriptions upon special terms may be counted if the special terms are void or unenforceable, and the subscrip-

<sup>746</sup> Ante, § 459.

<sup>747</sup> Ante, § 459.

<sup>748</sup> Ante, § 465 et seq. 749 Lewey's Island R. Co. v. Bolton, 48 Me. 451, 77 Am. Dec. 236; Ticonic Water Power & Manufacturing Co. v. Lang, 63 Me. 480; Proprietors of Cabot & West Springfield Bridge v. Chapin, 6 Cush.

<sup>751</sup> Rutland & Burlington R. Co. v. Russell, 88 Cal. 277. v. Thrall, 35 Vt. 536.

ton, 48 Me. 451, 77 Am. Dec. 236, (Ky.) 219.

a subscription for preferred stock which was to draw ten per cent. interest at once was excluded in determining whether the required amount of stock had been subscribed.

<sup>752</sup> Troy & Greenfield R. Co. v. Newton, 8 Gray (Mass.) 596; New York, Housatonic & M. R. Co. v. (Mass.) 500.

The first state of the first state of

Contra, Phillips v. Covington & In Lewey's Island R. Co. v. Bol- Cincinnati Bridge Co., 2 Metc.

tion valid, as in the case of an oral stipulation which is inadmissible to add to or vary a written subscription.753

Unauthorized subscription as agent.—A subscription made by a person as agent for another without authority, and not ratified, may be counted in those states in which it is held that the person thus assuming to act as agent without authority becomes liable himself, not merely in damages, but as a subscriber;754 but such a subscription cannot be counted in those states in which this doctrine is not recognized. For this purpose, a mere liability to the corporation in damages is not equivalent to a subscription.<sup>755</sup> Of course, a subscription may be counted, notwithstanding it was made by a person as agent for another without authority, if it has been ratified by the latter, so as to be binding on him.756

Evidence.—As we have seen in a former section, the records of a corporation are competent and sufficient evidence to prove subscriptions to its capital stock, and to show whether or not the amount of stock required by its charter has been subscribed, where no proof is introduced to destroy their effect. 757 And a certificate by the commissioners appointed to receive subscriptions, and to certify when the required amount of stock has been subscribed, is conclusive on the subscribers.758

A resolution by the directors of a railroad company that sufficient stock has been subscribed to build the road, if passed by them in good faith, renders a person liable on a subscription

753 Ridgefield & New York R. Co. Dec. 363. v. Brush, 43 Conn. 86. See ante, Southern Hotel Co. v. Russell, 88 § 467(c).

754 State v. Smith, 48 Vt. 266. And see National Commercial Bank v. McDonnell, 92 Ala. 387; Allibone v. Hager, 46 Pa. St. 48.

A subscription made by a partner in the name of the firm may be counted, whether he had authority to bind the firm or not, since, if the firm is not bound, he is bound individually. Union Hotel Co. v. Hersee, 79 N. Y. 454, 35 Am. Rep.

755 Salem Mill Dam Corp. v. Ropes, 9 Pick. (Mass.) 187, 19 Am.

And see California Cal. 277.

756 Ante, § 449(a). But see California Southern Hotel Co. v. Russell, 88 Cal. 277.

757 Ante, § 454.

Articles of association of a corporation, certified by the secretary of state, are prima facie evidence of the fact that the full amount of the capital stock required by the articles has been subscribed. Jewell v. Rock River Paper Co., 101

758 Ante, § 454.

to stock in the company made upon condition that such an amount of stock should be subscribed as should, in the judgment of the directors, be sufficient for the construction of the road.<sup>759</sup>

Where, in a petition to recover a subscription to the stock of a corporation, it is averred that the directors had been duly elected by the stockholders, in pursuance of notice, it is to be presumed that the requisite amount of stock had been subscribed to authorize such election, and also to authorize the commencement of business, and the making of assessments by the directors so elected.760

# § 507. Waiver and estoppel.

A condition, express or implied, that the full amount of the capital stock, or a certain percentage thereof, shall be subscribed before the subscribers shall be liable on their subscriptions, may be waived by a subscriber, and the waiver may be either express or implied.<sup>761</sup> And aside from any question of waiver in the proper sense, a subscriber may be estopped from setting up nonperformance of the condition. 762 A waiver will generally be implied, or else the subscriber will be estopped, if, with knowledge of nonperformance of the condition, he has participated in or consented to the letting of contracts, the creation of debts, or the doing of any other corporate act which involves the necessity of calling for payment of subscriptions. 763

C. Ry. Co., 80 Pa. St. 31. 760 Ashtabula & New Lisbon R. Co. v. Smith, 15 Ohio St. 328.

761 Anderson v. Middle & East Tennessee Central R. Co., 91 Tenn. 44; Macfarland v. West Side Improvement Ass'n, 56 Neb. 277; and other cases cited in the notes following.

762 Bavington v. Pittsburgh & Steubenville R. Co., 34 Pa. St. 358; Montpelier & Wells River R. Co. v. Langdon, 45 Vt. 137; and other cases in the notes following.

<sup>763</sup> Anderson v. Middle & East Tennessee Central R. Co., 91 Tenn. 44; Hutchins v. Smith, 46 Barb. An officer of a corporation who, (N. Y.) 235; Hamilton v. Clarion, by an agent to whom he has dele-

750 Cass v. Pittsburg, Virginia & Mahoning & P. R. Co., 144 Pa. St. 34; California Southern Hotel Co. v. Callender, 94 Cal. 120, 28 Am. St. Rep. 99; New Hampshire Central R. Co. v. Johnson, 30 N. H. 390, 64 Am. Dec. 300; Hager v. Cleveland, 36 Md. 476; Musgrave v. Morrison, 54 Md. 161; Garling v. Boechtel, 41 Md. 305; Morrison v. Dorsey, 48 Md. 461; Masonic Temple Ass'n v. Channell, 43 Minn. 553; International Fair & Exposition Ass'n v. Walker, 83 Mich. 386; Gibbons v. Ellis, 83 Wis. 434; Centre & Kishacoquillas Turnpike Road Co. v. McConaby, 16 Serg. & R. (Pa.) 140.

A waiver may also be implied if a subscriber, with knowledge that the condition has not been performed, pays his subscription or a part thereof, or gives his unconditional note therefor, or if he acts as a stockholder or officer of the corporation in doing business, or participates in corporate meetings, etc., 764 unless the circumstances are such as to show that there was no intention to waive performance of the condition, and not to operate as an estoppel. Mere presence of a subscriber at a stockholders' meeting as a spectator, without taking any part therein, will not operate as a waiver or estoppel.<sup>766</sup>

A subscriber for stock prior to incorporation, on condition that the full amount of stock shall be subscribed, or a certain percentage thereof, before organization, waives such condition if he participates or acquiesces in the organization of the cor-

gated performance of his duties, has received subscriptions and disbursed money in the business of the corporation, is chargeable, by virtue of his office, with notice of a deficiency in stock subscriptions, and is estopped to set up such deficiency to escape liability for assessments on his subscription. Macfarland v. West Side Improve-

ment Ass'n, 53 Neb. 417. 764 Dayton & Cincinnati R. Co. v. 764 Dayton & Cincinnati R. Co. V. Hatch, 1 Disn. (Ohio) 84; Chamberlain v. Painesville & Hudson R. Co., 15 Ohio St. 225; California Southern Hotel Co. v. Callender, 94 Cal. 120, 28 Am. St. Rep. 99; Cole v. Satsop R. Co., 9 Wash. 487, 43 Am. St. Rep. 858; Cornell's Appeal, 114 Pa. St. 153; O'Donald v. Evansville, I. & C. Straight Line R. Co. 14 Ind. 250; McAllister v. In-Co., 14 Ind. 259; McAllister v. Indianapolis & Cincinnati R. Co., 15 Ind. 11; Evansville, f. & C. Straight Line R. Co. v. Dunn, 17 Ind. 603; Slipher v. Earhart, 83 Ind. 173; Union Hotel Co. v. Hersee, 79 N. Y. 454, 35 Am. Rep. 536; Ind. 173; Union Hotel Co. v. Hersee, 79 N. Y. 454, 35 Am. Rep. 536; position Ass'n v. Walker, 88 Mich. Masonic Temple Ass'n v. Channell, 62; Id., 97 Mich. 159. See, also, 43 Minn. 353; Auburn Opera Hards v. Platte Valley Improve-House & Pavilion Ass'n v. Hill, 113 Cal. 382; International Fair & 766 New Hampshire Central R. Exposition Ass'n v. Walker, 83 Co. v. Johnson, 30 N. H. 390, 64 Mich. 386; Craig v. Cumberland Am. Dec. 300.

Valley State Normal School, 72 Pa. St. 46.

A subscriber who was also a commissioner to receive subscriptions, and who has recited in his certificate subscription of the required amount of stock, is estop-

ped to deny the fact. See Bavington v. Pittsburgh & Steubenville R. Co., 34 Pa. St. 358.

765 Portland & Fairview R. Co. v. Spillman, 23 Or. 587; Ridgefield & New York R. Co. v. Reynfield & New York R. Co. v. Reynfield olds, 46 Conn. 375; Parker v. Thomas, 19 Ind. 213, 81 Am. Dec. 385; Atlantic Cotton Mills v. Abbott, 9 Cush. (Mass.) 423; Garling v. Boechtel, 41 Md. 305.

Where a subscriber attended one of the corporate meetings, and voted his stock, but afterwards refused to receive a certificate or pay assessments on his stock, it was held that whether he waived a condition that the whole capital stock should be subscribed was for

poration without compliance therewith. 767 Acts done by a subscriber in the belief that the condition has been performed cannot operate as a waiver or estoppel. 768

### XI. PAYMENTS ON SUBSCRIPTIONS.

§ 508. In general.—Payment of subscriptions, or of a certain percentage thereof, is sometimes expressly required as a condition precedent to incorporation, or to the right to commence business; but it is not necessary unless expressly required.

By the weight of authority, failure to comply with a statutory requirement that a certain percentage of subscriptions shall be paid at the time of subscribing cannot be set up by a subscriber to escape liability on his subscription. The contrary, however, is held in some states in the case of subscriptions prior to incorporation.

#### Effect of nonpayment on legality of incorporation, or § 509. right to commence business.

A statute authorizing the formation of a corporation may require subscribers for stock therein to pay the whole or a certain percentage of their subscriptions as a condition precedent to acquiring a legal corporate existence. If such an intention appears, a de jure corporation cannot be formed without the required payments being made. If it is attempted to be formed without such payments, and the association assumes to exercise corporate powers, it will be ousted in quo warranto proceedings by the state, 769 and all the other consequences of failure to acquire legal corporate existence will follow.770

767 California Southern Hotel Co. v. Callender, 94 Cal, 120, 28 Am. St. Rep. 99.

768 Portland & Fairview R. Co. v. Spillman, 23 Or. 587; Denny Hotel Co. v. Gilmore, 6 Wash. 152; Birge v. Browning, 11 Wash. 249; Orynski v. Loustaunan (Tex.) 15 S. W. 769 People v. Chambers, 42 Cal.

As to what constitutes a sufficient payment, see post, § 511.

770 Napier v. Poe, 12 Ga. 170; Jersey City Gas Co. v. Dwight, 29 N. J. Eq. 242.

A statute authorizing the formation of a railroad company or other 674; Johnson v. Schar, 9 S. D. 536; corporation, and requiring that at Hawkins v. Citizens' Real Estate least a certain amount of stock for & Investment Co. (Or.) 64 Pac. every mile of the proposed road 320. shall be subscribed, and ten per

Payment of subscriptions, or of a part thereof, may also be required as a condition precedent to the right to commence business or contract debts.771

Such payment, however, is not a condition precedent, either to legal incorporation, or to the right to commence business, unless it is expressly so provided.<sup>772</sup>

Where payment is required merely as a condition precedent to the right to commence business, or contract debts, nonpayment, while it may render the charter of the corporation subject to forfeiture by the state, does not affect the existence of the corporation.773

# § 510. Effect of nonpayment on validity of subscriptions, and liability of subscribers.

(a) In general.—The validity and binding effect of subscriptions for stock in a corporation, whether they are made after or before the corporation is formed, is clearly not in any way affected by failure of the subscribers to pay the whole or part of the same, unless payment is expressly required by the charter or enabling act or the articles of association.774 Whether such

shall be filed, is complied with if the aggregate amount of payments amounts to ten per cent. of one thousand dollars for each mile of the proposed road. It is not required that each subscriber shall pay ten per cent. on his subscription. Lake Ontario, Auburn & N. Y. R. Co. v. Mason, 16 N. Y. 451; Beattys v. Town of Solon, 64 Hun (N. Y.) v. Town of Solon, 64 Hun (N. 1.)
120; Troy & Rutland R. Co. v.
Kerr, 17 Barb. (N. Y.) 581; Eastern
Plank Road Co. v. Vaughan, 20
Barb. (N. Y.) 155; Ogdensburgh,
Rome & C. R. Co. v. Frost, 21
Barb. (N. Y.) 541; Spartanburg &
Asheville R. Co. v. Ezell, 14 S. C.

771 Wechselberg v. Flour City Nat. Bank, 24 U. S. App. 308, 64 Fed. 90; Tramwell v. Pennington, 45 Ala. 673.

772 Stokes v. Findlay, 4 McCrary,

cent. paid thereon in good faith, be- 205, Fed. Cas. No. 13,478; Young fore the articles of incorporation Reversible Lock-Nut Co. v. Young Lock-Nut Co., 72 Fed. 62; Smith v. Tallassee Branch of Central Plank-Road Co., 30 Ala. 650; New Haven & Derby R. Co. v. Chapman, 38 Conn. 56; Town of Searcy v. Yarnell, 47 Ark. 269; Mitchell v. Rome R. Co., 17 Ga. 574; Hammond v. Straus, 53 Md. 1; Chase's Patent Elevator Co. v. Boston Tow-Boat Co., 152 Mass. 428; Mc-Ginty v. Athol Reservoir Co., 155 Mass. 183; Singer Mfg. v. Peck, 9 S. D. 29; Blair v. Rutherford, 31 Tex. 465; National Bank of Jef-ferson v. Texas Investment Co., 74 Tex. 421.

> 778 Young Reversible Lock-Nut Co. v. Young Lock-Nut Co., 72 Fed. 62; Baker v. Backus' Adm'r, 32 III. 79; Hammond v. Straus, 53 Md. 1; Staunton Copper Mining Co. v. Thurmond, 7 Mo. App. 587.

failure renders a subscription invalid when payment is expressly required depends upon the purpose of the requirement and the intention.

When the charter of a corporation or the enabling act under which it is organized clearly requires that a certain percentage of subscriptions shall be paid as a condition precedent to incorporation, there can be no liability on subscriptions in the absence of such payment, unless the subscriber can be held estopped to deny legal incorporation, 775 for a subscription cannot be binding until the corporation is in existence.<sup>776</sup>

This cannot apply where payments on subscriptions are not required as a condition precedent to becoming incorporated, but merely for the purpose of providing funds for preliminary expenses, or as a condition precedent to engaging in business or contracting debts.777

(b) Failure of subscriber to pay required deposit at time of subscribing.—(1) Subscriptions after incorporation.—In so far as subscriptions after the corporation has been organized are concerned, a charter or statutory requirement that a certain amount or percentage shall be paid at the time of subscribing is to be construed as intended merely for the benefit of the corporation, so that it may be waived by it, unless a contrary intention clearly appears. As a rule, failure to make the required payment cannot be set up by a subscriber to escape liability on his subscription, unless subscriptions without such payment are expressly prohibited or declared to be void.778

proceed to the transaction of business, a certain percentage of its Co. v. Donovan, 57 Mich. 318. capital stock should be subscribed and paid in, the requirement that Co. v. Bassett, 20 Minn. 535, 18 such amount should be actually Am. Rep. 376. See, also, Oler v. paid in was held not a condition Faltimore & Randallstown R. Co.,

v. Dwyer, 49 Iowa, 121; Wheeler v. precedent to the company's right Millar, 90 N. Y. 353; Schaeffer v. to enforce payment of calls on Missouri Home Ins. Co., 46 Mo. subscriptions. McDermott v. Don-248; ante, § 383. And see the egan, 44 Mo. 85. See, also, Branch cases cited in the notes following.

775 Post, § 515.

775 Post, § 515.

775 Post, § 515. 777 Where a charter provided that, before the corporation should proceed to the transaction of the transacti

It was so held in a Minnesota case, where the charter of a railroad company provided that its capital stock should be two million dollars, divided into shares of one hundred dollars each, and that five dollars should be paid on each share at the time of subscribing. It was held that a subscriber could not set up his failure to make the payment in an action by the corporation on the subscription. "If the plaintiff," it was said, "sees fit to accept the subscription, without requiring the concurrent payment which it is authorized to require, this is a waiver of its right to insist upon such payment, a waiver to which the subscriber assents and agrees by the very act of subscription without concurrent payment. In the absence of any rule of law or' provision of statute, forbidding a waiver, or invalidating any subscription made upon a waiver, this indulgence upon the part of the company cannot be turned against it, as a defense to an action to recover the subscription price of shares."779

If the charter or statute expressly forbids subscriptions to be taken without payment of a certain amount, or a certain percentage thereof, or expressly declares that they shall be void, a subscription without such payment is absolutely void, and cannot be enforced.780

Eastern Shore R. Co., 77 Md. 92, 39 Am. St. Rep. 396; Elysville Mfg. Co. v. Okisko Co., 5 Md. 152; Montpelier & Wells River R. Co. v. Langdon, 46 Vt. 284; Mitchell v. Rome R. Co., 17 Ga. 574; Selma & Tennessee R. Co. v. Rountree, 7 Ala. 670; Ryder v. Alton & Sangamon R. Co., 13 Ill. 517; Pittsburgh, mon R. Co., 13 III. 517; Pittsburgh, Wheeling & K. R. Co. v. Applegate, 21 W. Va. 172. And see the dictum in Taggart v. Western Maryland R. Co., 24 Md. 563, 89 Am. Dec. 760; Jenkins v. Union Turnpike Road, 1 Caines Cas. (N. Y.) 86; Beach v. Smith, 30 N. Y. 116, 132.

In Galveston Hotel Co. v. Bolton, 46 Tex. 633, it was held that, where the charter of a corporation provides that ten per cent. of the

41 Md. 583; Webb v. Baltimore & ited with the treasurer at the time of the subscription, a subscriber may show, in an action on his subscription, that he did not pay the ten per cent., as tending to show that there was not a complete contract of subscription.

779 Minneapolis & St. Louis Ry. Co. v. Bassett, 20 Minn. 535, 18 Am. Rep. 376.

<sup>780</sup> Black River & Utica R. Co. v. Clarke, 25 N. Y. 208; Beach v. Smith, 28 Barb. (N. Y.) 254, 30 N. Y. 116; New York & Oswego Midland R. Co. v. Van Horn, 57 N. Y. 473; South Buffalo Natural Gas Co. v. Bain, 9 Misc. Rep. (N. Y.) 425; Charlotte & South Carolina R. Co. v. Blakely, 3 Strob. (S. C.) 245; McRae v. Russel, 12 Ired. (N. C.) 224.

In General Electric Co. v. Wightamount subscribed shall be depos- man, 3 App. Div. (N. Y.) 118, it

Provisions not applicable to subscriptions after organization.—Under a statute authorizing the formation of a corporation, which appointed commissioners to open books and receive subscriptions to its capital stock, and provided that, on their certificate to the governor that a certain amount of stock was subscribed, he should issue letters patent erecting the subscribers into a corporation, the court held that a requirement therein that a certain amount should be paid to the commissioners on each share at the time of subscribing, while it required such payment on all subscriptions received by the commissioners, and which were necessary to authorize the issuance of letters patent, did not apply to subscriptions received by the corporation itself after its creation.<sup>781</sup>

And where a statute providing for the formation of corporations required, in one section, that a certain amount should be paid to the commissioners at the time of subscribing, and provided, in another section, that, after the organization of a corporation thereunder, it should have the power to enlarge its stock by new subscriptions, in such manner and form as it should think proper, it was held that no payment at the time of subscribing was required on subscriptions after organization.<sup>782</sup>

---(2) Subscriptions prior to incorporation.—The courts have not agreed in construing charter or statutory provisions requiring payment of a certain percentage of subscriptions made prior to the organization of a corporation. Some of the courts have held that, where the charter or statute merely requires such payment, without expressly prohibiting subscriptions without pay-

scribe for shares of stock in a corporation which had not been issued was in violation of the policy of a statute requiring subscribers to pay in money, at the time of subscribing, ten per cent. of the amount subscribed, and was there-

Where no stock book is shown to have been kept, but it appears

was held that a contract to sub- a portion of the shares were taken. it will be presumed, in the absence of any showing to the contrary, that the amount required by the articles of incorporation was paid. Sweney v. Talcott, 85 Iowa, 103.

> 781 Philadelphia & West Chester R. Co. v. Hickman, 28 Pa. St. 318. And see Montpelier & Wells River R. Co. v. Langdon, 46 Vt. 284.

from the minutes of different 782 Erie & Waterford Plank meetings of the stockholders that Road Co. v. Brown, 25 Pa. St. 156.

ment, or declaring that they shall be void, a subscriber's failure to comply with the requirement does not render his subscription void, and cannot be set up by him to defeat an action thereon. These decisions are based either upon the ground that the failure of the subscriber to make the payment is wrongful, and that he should not be permitted to take advantage of his own wrong for the purpose of escaping liability on his subscription, or on the ground that the requirement is intended for the benefit of the corporation, rather than of the public, and that it may therefore be waived by the corporation, or by the commissioners receiving the subscription, who act as its agents, or on both grounds,783

Other courts have taken a contrary view, and have construed the requirement as intended, not merely for the benefit of the corporation, but for the protection of the public, to prevent the subscription list from being filled up with names of nominal stockholders, and the irresponsible creatures of others.<sup>784</sup> these courts have held, therefore, that the requirement cannot be waived by the corporation or the agents receiving subscriptions, and that a subscription upon which the required deposit is not paid is illegal and void, and no action can be maintained upon it.785

783 Wight v. Shelby R. Co., 16 Pittsburgh, Wheeling & K. R. Co. v. B. Mon. (Ky.) 4, 63 Am. Dec. 522; Applegate, 21 W. Va. 172. Canal Bank v. Holland, 5 La. Ann. 363; Vicksburg, Shreveport & T. 363; Vicksburg, Shreveport & T. Turnpike Road v. Henderson, 8 R. Co. v. McKean, 12 La. Ann. 638; Serg. & R. (Pa.) 219, 11 Am. Dec. Red River R. Co. v. Young, 6 Rob. (La.) 39; Illinois River R. Co. v. Zimmer, 20 Ill. 654; Stuart v. Valley R. Co., 32 Grat. (Va.) 146; Henderson, 8 Serg. & R. (Pa.) 219, 11 Am. Dec. 593; Leighty v. Sussmith v. Tallassee Branch of Central Plank-Road Co., 30 Ala. Co., 14 Serg. & R. (Pa.) 434; 650; Selma & Tennessee R. Co. v. Boyd v. Peach Bottom Ry. Co., 90

784 Per Gibson, J., in Hibernia Turnpike Road v. Henderson, 8

Rountree, 7 Ala. 670. See, also, Pa. St. 169; Union Turnpike Road Minneapolis & St. Louis Ry. Co. v. v. Jenkins, 1 Caines (N. Y.) 381, Bassett, 20 Minn. 535, 18 Am. Rep. 1 Caines' Cas. 86; Goshen & Mini-Bassett, 20 Minn. 535, 18 Am. Rep. 1 Cames Cas. 86; Gosnen & Minn. 376; Henry v. Vermillion & Ashland R. Co., 17 Ohio, 187; Chamberlain v. Painesville & Hudson Turnpike Co. v. McKean, 11 R. Co., 15 Ohio St. 225; Haywood Johns. (N. Y.) 98; Excelsior Grain & Pittsborough Plank Road Co. Binder Co. v. Stayner, 25 Hun (N. v. Bryan, 6 Jones (N. C.) 82; Mc-Y.) 91, 61 How. Pr. 456; Taggart Rae v. Russel, 12 Ired. (N. C.) 224; v. Western Maryland R. Co., 24

In a Pennsylvania case, an act to incorporate a turnpike company appointed commissioners to open books and receive subscriptions, and provided that, when fifty or more persons should subscribe two hundred shares of the stock, the commissioners should certify to the governor the names of the subscribers, and the number of shares subscribed by each, whereupon the governor should issue letters patent erecting the subscribers and those who might afterwards subscribe into a corporation. It also provided that every person offering to subscribe in the said books, in his own or any other name, should previously pay to the commissioners the sum of five dollars for each and every share to be subscribed, out of which should be defrayed the expense of taking the subscription and other incidental charges, and the remainder paid over to the corporation when organized. It was held that this provision was not intended merely for the benefit of the corporation, or merely to raise money for expenses preliminary to organization, but for the protection of the public against subscriptions by persons without ability to pay, and persons who might subscribe for the purpose of speculation merely, and that subscriptions on which the required payment was not made were illegal and void.786

Md. 563, 89 Am. Dec. 760; State future time. Napier v. Poe, 12 Ga. Ins. Co. v. Redmond, 1 McCrary, 170.
308, 3 Fed. 764; Fiser v. Mississip Under the New York business ji & Tennessee R. Co., 32 Miss. 359. See, also, Black River & Utica R. Co. v. Clarke, 25 N. Y. 208; Beach v. Smith, 30 N. Y. 116; New York & Oswego Midland R. Co. v. Van Horn, 57 N. Y. 473.

Where the charter of a corporation required the commissioners.

tion required the commissioners appointed to receive subscriptions and organize the corporation to give notice for the election of directors as soon as the specified amount of stock should be subscribed, and a certain per cent. of each subscription paid, it was held

corporations law (sections 41-43), subscribers must pay ten per cent. on subscriptions after incorporation, but not on subscriptions prior thereto. United Growers' Co. v. Eisner, 22 App. Div. (N. Y.) 1; Yonkers Gazette Co. v. Taylor, 30 App. Div. (N. Y.) 334.

786 Hibernia Turnpike Road v. Henderson, 8 Serg. & R. (Pa.) 219, 11 Am. Dec. 593. Compare Hanover Junction & Susquehanna R. Co. v. Grubb, 82 Pa. St. 36.

Failure to pay the required deposit may be cured by the legisthat it did not require the payment lature, and it is cured by a statute of such proportion of subscripproviding that all defects and irtions at the time of subscribing, regularities in the proceedings of and that the commissioners might the commissioners in taking subreceive subscriptions payable at a scriptions to the stock shall be

If a charter or statute expressly declares that subscriptions shall be void unless a payment is made at the time of subscribing, a subscription without such payment cannot be enforced. 787 And the same is true where there is an express prohibition against taking subscriptions without such payment. 788

Even in Pennsylvania, where it is held that nonpayment of a deposit as required by a charter or general law renders a subscription illegal and void, it has been held that a subscriber is estopped to set up his failure to pay to defeat an action on his subscription, if he has exercised the rights and privileges conferred upon him thereby, and acted as a stockholder.789

A subscriber who transfers his stock to another, and thus treats it as valid, is estopped to deny that the payment necessary to give his subscription validity was made. 790

(3) Requirement in by-law.—A by-law of a corporation requiring a certain percentage of subscriptions to be paid at the time of subscribing, and declaring that subscriptions without such payment shall be void, is for the benefit of the corporation only, and does not render subscriptions absolutely void because

cured, and that such proceedings ment for stock. Blair v. Ruthershall be valid as though the statute ford, 31 Tex. 465. relating to such acts had been the contrary, under a New York statute, New York & Oswego Midland R. Co. v. Van Horn, 57 N. Y. 473.

Where a clause in a charter of a railroad company provided that the board of commissioners should receive no subscription to stock receive no subscription to stock Road Co. v. Brown, 25 Pa. St. 156. unless a certain per cent. thereof And see Clark v. Monongahela in cash should be paid at the time Navigation Co., 10 Watts (Pa.) of subscription, and that, if they 364; Garrett v. Dillsburg & Mcshould receive subscriptions with-chanicsburg R. Co., 78 Pa. St. 465; out such payment, they should be personally liable to pay the same, Road Co. v. Bryan, 6 Jones (N. C.) it was held that the fact that the 82; Greenville & Columbia R. Co. the commissioners did not exact v. Woodsides, 5 Rich. Law (S. C.) the required payment from sub-145 55 Am Dec 708 the required payment from subscribers afforded no defense to a note given by a stockholder in pay
Philadelphia R. Co., 28 Pa. St. 339.

787 Charlotte & South Carolina fully complied with. Clark v. Mo-R. Co. v. Blakely, 3 Strob. (S. C.) nongahela Navigation Co., 10 245; McRae v. Russel, 12 Ired. (N. Watts (Pa.) 364. See, however, to C.) 224; Wood v. Coosa & Chat-

C.) 224, WOOD V. COOSE & CHEV tooga River R. Co., 32 Ga. 273. 788 Black River & Utica R. Co. v. Clarke, 25 N. Y. 208; Beach v. Smith, 28 Barb. (N. Y.) 254, 30 N. Y. 116; New York & Oswego Midland R. Co. v. Van Horn, 57 N. Y.

789 Erie & Waterford Plank-Road Co. v. Brown, 25 Pa. St. 156.

of nonpayment of the required amount. The corporation, if it sees fit, may treat them as valid, and, if it does so, the subscribers are bound.791

## § 511. Sufficiency of payment.

The deposit must be paid in money or its equivalent, whether a payment in "cash" or in "money" is expressly required or not. for otherwise it would be an easy matter to evade the statute.<sup>792</sup> Sometimes there is an express requirement to this effect.

Giving a promissory note for the amount required by a statute to be paid on a subscription is not a compliance with the stat-But a payment in goods or services for which the corporation has the power to contract, under an agreement entered into at the time of subscribing, is sufficient. 794

Giving a check for the amount of the deposit is not sufficient, where the drawer has no funds to meet the same, or where the check is not given in good faith, but for the purpose of evading the requirement, and without any intention that it shall be presented for payment, or where payment is countermanded before its presentment.<sup>795</sup> It is otherwise, however, if a check is given in good faith, and is presented and paid.<sup>796</sup>

791 Piscataqua Ferry Co. v. Jones, 39 N. H. 491. Compare State Ins. Co. v. Redmond, 1 McCrary, 308, 3 Fed. 764.
792 See Boyd v. Peach Bottom Ry. Co., 90 Pa. St. 169, and other

cases in the notes following.

793 Leighty v. Susquehanna & Waterford Turnpike Co., 14 Serg. & R. (Pa.) 434; Boyd v. Peach Bottom Ry. Co., 90 Pa. St. 169; In Waterford Turnpike Co., 14 Serg. Cal. 201.

& R. (Pa.) 434; Boyd v. Peach
Bottom Ry. Co., 90 Pa. St. 169; In Transit R. Co., 38 Hun (N. Y.)

re McKinley-Lanning Loan & 381; Rothchild v. Hoge, 43 Fed.

Trust Co., 12 Pa. Co. Ct. 40. Compare McRae v. Russel, 12 Ired.

(N. C.) 224.

Where a statute required pay-

794 Beach v. Smith, 28 Barb. (N. Y.) 254, 30 N. Y. 116; State v. Wood, 13 Mo. App. 139.

voou, 13 MO. App. 139.

795 Crocker v. Crane, 21 Wend.
(N. Y.) 211, 34 Am. Dec. 228; Excelsior Grain Binder Co. v. Stayner, 25 Hun (N. Y.) 91, 61 How.
Pr. 456; People v. Chambers, 42
Cal. 201.

But it has been held that a subment of ten per cent. in cash on scriber who has given his note in subscriptions prior to the filing of payment is estopped to set up articles of incorporation, it was such fact to escape liability. held that payment on a subscrip-Selma & Tennessee R. Co. v. tion by a certified check on the Rountree, 7 Ala. 670; Franklin v. 13th of the month was a good pay-Twogood, 18 Iowa, 515. And see ment, where the check was depositante, § 385, and cases there cited. ed on the 14th, and credited to the

Though a statute may expressly or impliedly require payment of a deposit at the time of subscribing, payment after subscribing is sufficient to render a subscription valid. 797 Under a statute providing that no subscription shall be taken without a payment of a certain amount thereof, a subscription is binding if payment of the deposit is made under legal compulsion, as where a judgment is recovered therefor, and paid or collected. 798

A subscription is not rendered invalid by failure to actually pay the deposit, where the subscriber is one of the commissioners to take subscriptions and receive the money required to be paid.<sup>799</sup> Where one of the commissioners to receive subscriptions makes a subscription in his own behalf, and credits the company in his account subsequently rendered to it with the amount of the deposit required to be paid, the subscription is binding.800

XII. OVERSUBSCRIPTION AND APPORTIONMENT OR DISTRIBUTION OF STOCK.

In general.—A subscription in excess of the authorized capital stock of the corporation is void, and cannot be enforced either by the corporation or by creditors.

When commissioners are appointed to receive subscriptions and to apportion or distribute the stock in case of an excessive sub-

Where a statute required a certain amount of stock to be subscribed and paid in cash, it was held that the giving of checks by subscribers in good faith on banks in which there were funds, and which would have been paid if presented, was a substantial and sufficient compliance with the statute, although the checks were not in fact presented because the R. Co., 13 Ill. 516; Grayble v. York money was not needed, and were & Gettysburg Turnpike Road Co., afterwards returned to the draw- 10 Serg. & R. (Pa.) 269. See, also, ers on their payment of the money. Beach v. Smith, 28 Barb. (N. Y.) People v. Stockton & Visalia R. 254, 30 N. Y. 116. Co., 45 Cal. 306, 13 Am. Rep. 178. Son Beach v. Smith, 28 Barb. (N. 797 Black River & Utica R. Co. Y.) 254, 30 N. Y. 116.

payee on the 15th, although the v. Clarke, 25 N. Y. 208; Beach v. articles of incorporation were filed Smith, 28 Barb. (N. Y.) 254, 30 N. on the 14th. In re Staten Island Y. 116; Klein v. Alton & Sanga-Rapid Transit R. Co., 38 Hun (N. y.) 381.

Y. 116; Klein v. Alton & Sanga-Rapid Transit R. Co., 38 Hun (N. selma & Tennessee R. Co., 6 Ala. Ogdensburgh, Clayton 741; Rome R. Co. v. Wooley, 3 Abb. Dec. (N. Y.) 398; Fiser v. Mississippi & Tennessee R. Co., 32 Miss.

<sup>798</sup> Ogdensburgh, Clayton & Rome R. Co. v. Wooley, 3 Abb. Dec. (N. Y.) 398; Hall v. Selma & Tennessee R. Co., 6 Ala. 741.
799 Ryder v. Alton & Sangamon

scription, a valid distribution or apportionment is a condition precedent to liability on subscriptions. The distribution must be made by the commissioners as a board, and their powers cannot be delegated.

## § 513. Effect of oversubscription.

As was shown in a former chapter, a corporation has no power to increase its capital stock without legislative authority,801 and therefore, if it receives subscriptions in excess of its authorized capital stock, they are without consideration and void, and cannot be enforced either by the corporation or by creditors. such a case, the subscriber is not estopped. 802 The mere fact, however, that the promoters of a corporation, before incorporation, received subscriptions in excess of the authorized capital stock, is altogether immaterial if the corporation, when organized, does not accept the excessive subscriptions. A plea in an action on a subscription, therefore, does not set up any defense, and is demurrable, where it alleges merely that the promoters received subscriptions in excess of the authorized capital stock, without showing that the excessive subscriptions were accepted by the corporation, so as to enter into its capital stock.803

# § 514. Distribution or apportionment by commissioners.

Where commissioners are appointed to receive subscriptions to the capital stock of a corporation to be formed, until a certain sum is subscribed, and are then required to call a meeting of the stockholders to elect directors, they have no power to make a proportionate deduction of all shares subscribed, without reference to the priority of subscription, when excessive sub-

<sup>801</sup> Ante, § 407. 802 Scovill v. Thayer, 105 U. S. Bristol Creamery Co. v. Tilton (N. 143, 2 Keener's Cas. 897; Mack-H.) 47 Atl. 591. And see ante, § ley's Case, 1 Ch. Div. 247; Lath-407(g). rop v. Kneeland, 46 Barb. (N. Y.) 432; Burrows v. Smith, 10 N. Y. R. Co., 41 Md. 583; Level Land more & Randallstown R. Co., 41 Co. v. Hayward, 95 Wis. 109; Md. 583.

Kampman v. Tarver, 87 Tex. 491;

<sup>550;</sup> Clark v. Turner, 73 Ga. 1; Co., 15 Ind. App. 329, 57 Am. St. Oler v. Baltimore & Randallstown Rep. 230. See, also, Oler v. Balti-

scriptions are received, but their authority is limited to receiving subscriptions up to the authorized amount. 804 The commissioners, however, may be authorized to receive subscriptions in excess of the authorized capital stock, and then to apportion or distribute the stock among the subscribers, and they may be given a discretion in the distribution.805

When commissioners are appointed to receive subscriptions for stock in a corporation to be formed, and to apportion or distribute the stock among the subscribers in the case of oversubscription, a valid distribution of the stock is a condition precedent to the existence of the corporation, and to liability on subscriptions.<sup>806</sup> In an action on a subscription, however, the presumption, in the absence of evidence to the contrary, is that only the authorized amount of stock has been subscribed, and the burden is on the subscriber if he claims that excessive subscriptions have been received, and that there has been no distribution.807

Commissioners appointed to receive subscriptions and distribute the stock among the subscribers where more than the required amount of stock is subscribed, "in such manner as they

Eq. 333.

805 Haight v. Day, 1 Johns. Ch. (N. Y.) 18; Crocker v. Crane, 21 Wend. (N. Y.) 211, 34 Am. Dec. 228; Clarke v. Brooklyn Bank, 1 Edw. Ch. (N. Y.) 361; Walker v. Devereaux, 4 Paige (N. Y.) 229. Under an act of incorporation

authorizing commissioners to receive subscriptions, and "to apportion the excess of shares among the several subscribers, as they should judge discreet and proper, they are not required to make apportionments to each subscriber in proportion to the amount of his subscription. Haight v. Day, 1 Johns. Ch. (N. Y.) 18.

When they are given such discretion, their apportionment is final, if they act in good faith. Walker v. Devereaux, 4 Paige (N. Y.) 229.

804 Van Dyke v. Stout, 8 N. J. however, and act fraudulently or unjustly in distributing or apportioning stock, a person aggrieved may maintain a suit in equity for relief by injunction and reapportionment. Meads v. Walker, Hopk. Ch. (N. Y.) 587; Walker v. Devereaux, 4 Paige (N. Y.) 229.

806 Crocker v. Crane, 21 Wend. (N. Y.) 211, 34 Am. Dec. 228; Burrows v. Smith, 10 N. Y. 550; Walker v. Devereaux, 4 Paige (N. Y.) 229.

A check given for stock in a corporation which acquires no existence because the stock is not distributed by the number of commissioners required to constitute a legal board is void for want of consideration. Crocker v. Crane, 21 Wend. (N. Y.) 211, 34 Am. Dec. 228. See infra, this section.

1) 229. So Buffalo & New York City R. If they abuse their discretion, Co. v. Dudley, 14 N. Y. 336.

shall deem most conducive to the interests of the said corporation," act in a judicial capacity in distributing the stock, since they must exercise a discretion, and distribute the stock as may be most beneficial to the interests of the company, and therefore they cannot appoint an agent or deputy to make the distribution.808 A majority of the commissioners may decide any question within the scope of their powers, but, unless it is expressly provided that a majority shall constitute a quorum and have power to act, they must all be present at meetings. If a mere majority meet and distribute the stock, the proceeding is without jurisdiction, and void.809

As was shown in a former section, the powers and authority of the commissioners cease as soon as the corporation is organized and officers elected,810 and thereafter any apportionment or distribution of stock is to be made by the corporation.811

Fraud practiced by one of the commissioners upon his cocommissioners as to the distribution of stock, being in a matter as to which they act judicially, does not render their proceedings void as respects the subscribers, if they have jurisdiction in the premises.812 The effect of fraud or wrong on the part of the commissioners in refusing to allow persons to subscribe, and subscribing for all the shares themselves, is considered in another section.813

### XIII. ESTOPPEL OF SUBSCRIBERS.

§ 515. In general.—A subscriber for stock in a corporation is estopped to deny the existence of the corporation if he subscribed after its formation, but not where the subscription was prior to its formation, unless he has in some way participated in its forma-

has long been perfectly well set-tled," said Judge Cowen, in this case, "that where a statute constitutes a board of commissioners or other officers to decide any matter, but makes no provision that a majority shall constitute a

808 Crocker v. Crane, 21 Wend. quorum, all must be present to (N. Y.) 211, 34 Am. Dec. 228. hear and consult, though a ma-809 Crocker v. Crane, 21 Wend. jority may then decide." See Ex N. Y. 211, 34 Am. Dec. 228. "It parte Rogers, 7 Cow. (N. Y.) 526. 810 Ante, § 450(b).

811 State v. Lehre, 7 Rich. Law (S. C.) 234.

812 Crocker v. Crane, 21 Wend. (N. Y.) 211, 34 Am. Dec. 228.

813 Ante. § 450(b).

tion, or recognized or held it out as legally organized. If he has done this, he is generally estopped, whether the subscription was prior to or after incorporation.

A subscriber may also be estopped by allowing himself to appear as a stockholder or subscriber, by participating in the organization of the corporation, or by acting as a stockholder after organization—

- (1) To deny that he was a subscriber.
- (2) To allege that his subscription was invalid.
- (3) To set up a release or discharge from liability.
- (4) To set up nonperformance of conditions precedent.
- (5) Or to set up conditional delivery of his subscription.

By accepting and acting upon a subscription, the corporation and the other stockholders may be estopped to deny its validity.

Estoppel to deny corporate existence.—As was shown in a former chapter, it is a general principle, recognized in most jurisdictions, although not in all, that a person who contracts with an association as a corporation thereby admits and estops himself to deny its corporate existence, whether it be a corporation de facto or not.814 It has been held, therefore, that a person who subscribes for stock in an association as an existing corporation is thereby estopped to deny its legal corporate existence for the purpose of escaping liability on his subscription, not only as against creditors of the corporation or its receiver or assignee in bankruptcy,815 but also as against the corporation itself.816 A subscriber for stock who has given the corpora-

814 See ante, § 83 et seq., where v. Davis, 14 Johns. (N. Y.) 238, 7 is doctrine is discussed at Am. Dec. 459; Chester Glass Co. v. length.

815 Casey v. Galli, 94 U. S. 673; Chubb v. Upton, 95 U. S. 665; Upton v. Jackson, 1 Flip. 413, Fed. Cas. No. 16,802; Upton v. Hansbrough, 3 Biss. 417, Fed. Cas. No. 16,801; Hause v. Mannheimer, 67 Minn. 194; Ossipee Hosiery & Woolen Mfg. Co. v. Canney, 54 N. H. 295; Torras v. Raeburn, 108 Ga. 345; McCarthy v. Lavasche, 89 Ill. 270, 31 Am. Rep. 83; Reychaud v. Lane, 24 La. Ann. 404. v. Lane. 24 La. Ann. 404.

Am. Dec. 459; Chester Glass Co. v. Dewey, 16 Mass. 94, 8 Am. Dec. 128; South Bay Meadow Dam Co. v. 128; South Bay Meadow Dam Co. v. Gray, 30 Me. 547; Judah v. American Live Stock Ins. Co., 4 Ind. as. No. 16,802; Upton v. Hansrough, 3 Biss. 417, Fed. Cas. No. 6,801; Hause v. Mannheimer, 67 kinn. 194; Ossipee Hosiery & Voolen Mfg. Co. v. Canney, 54 N. I. 295; Torras v. Raeburn, 108 a. 345; McCarthy v. Lavasche, 89 l. 270, 31 Am. Rep. 83; Reychaud. Lane, 24 La. Ann. 404. tion a promissory note in payment of his subscription cannot escape liability thereon, either as against the corporation or, as against an assignee of the note, by denying the existence of the corporation on the ground that it was illegally organized beyond the limits of the state, or that it failed to comply with conditions precedent to legal incorporation, etc.<sup>817</sup>

A subscriber is not estopped, however, either as against the corporation or its creditors, if his subscription was prior to the organization of the corporation, and therefore conditional upon legal incorporation, unless he has participated in some way in the defective organization, or in holding out the corporation as legally organized.<sup>818</sup>

A subscriber for stock, whether after or before formation of the corporation, is estopped to deny the legality of its organization or its corporate existence, either as against creditors or as against the corporation itself, if he participated in its organization, or acquiesced therein with knowledge of the facts, or if he has recognized it as being legally organized, or if he has acted as an officer or stockholder or otherwise participated in holding it out to the public as a legally constituted cor-

& S. R. Co., 28 Mich. 272; Parker v. Northern Central Michigan R. Co., 33 Mich. 23; Lail v. Mt. Sterling Coal Road Co., 13 Bush (Ky.) 32; Ohio & Mississippi R. Co. v. McPherson, 35 Mo. 13, 86 Am. Dec. 128; Home Stock Ins. Co. v. Sherwood, 72 Mo. 461; National Commercial Bank v. McDonnell, 92 Ala. 387; McCune Mining Co. v. Adams, 35 Kan. 193; Ossipee Hosiery & Woolen Mfg. Co. v. Canney, 54 N. H. 295; Baile v. Calvert College Educational Society, 47 Md. 117; Ogden Clay Co. v. Harvey, 9 Utah, 497; Black River & Utica R. Co. v. Clarke, 25 N. Y. 208; Wilmington & Manchester R. Co. v. Saunders, 3 Jones (N. C.) 126; Wilmington, Charlotte & Rutherford R. Co. v. Thompson, 7 Jones (N. C.) 387; Montpelier & Wells River R. Co. v. Langdon, 46 Vt. 284; Hickling v. Wilson, 104 III. 54; Brownlee v.

Ind. 68; Mullen v. Beech Grove Driving Park, 64 Ind. 202; Cravens v. Eagle Cotton Mills Co., 120 Ind. 6, 16 Am. St. Rep. 298.

See, however, Hudson v. Green Hill Seminary Corp., 113 Ill. 618.

817 Camp v. Byrne, 41 Mo. 525; Goodrich v. Reynolds, 31 Ill. 490, 83 Am. Dec. 240; Bibb v. Hall, 101 Ala. 79. See, also, Ohio & Misissippi R. Co. v. McPherson, 35 Mo. 13, 86 Am. Dec. 128. Compare Haas v. Hall, 111 Ala. 442.

den Clay Co. v. Harvey, 9 Utah, 497; Black River & Utica R. Co. v. 463; Richmond Factory Ass'n v. Clarke, 25 N. Y. 208; Wilmington & Manchester R. Co. v. Saunders, ings Prospecting Co., 40 Neb. 470, 3 Jones (N. C.) 126; Wilmington, 42 Am. St. Rep. 677; Schloss v. Charlotte & Rutherford R. Co. v. Montgomery Trade Co., 87 Ala. 414, Thompson, 7 Jones (N. C.) 387; 13 Am. St. Rep. 51; Indianapolis Montpelier & Wells River R. Co. v. Furnace & Mining Co. v. Herkimer, Langdon, 46 Vt. 284; Hickling v. 46 Ind. 142, 1 Smith's Cas. 97, 1 Wilson, 104 Ill. 54; Brownlee v. Cum. Cas. 970; Rikhoff v. Brown's Ohio, Indiana & Illinois R. Co., 18 Rotary Shuttle Sewing Machine

poration.<sup>819</sup> Payment of a subscription or of an installment thereon will generally be a sufficient recognition of the legal existence of the corporation to operate as an estoppel.<sup>820</sup>

Estoppel to deny subscription, or the validity thereof.—If a person knowingly allows himself to appear as a subscriber and stockholder in a corporation, and, a fortiori, if he acts as a stockholder, by accepting a certificate of stock, making payments, and receiving dividends, or otherwise, he will be estopped

Co., 68 Ind. 388; Hudson v. Green Hill Seminary Corp., 113 Ill. 618; Henry v. Centralia & Chester R. Co., 121 Ill. 264; Hause v. Mannheimer, 67 Minn. 194; Birge v. Browning, 11 Wash. 249.

819 Chester Glass Co. v. Dewey, 16 Mass. 94, 8 Am. Dec. 128; Selma & Tennessee R. Co. v. Tipton, 5 Ala. 787, 39 Am. Dec. 344; McDonnell v. Alabama Gold Life Ins. Co., 85 Ala. 401; Lehman v. Warner, 61 Ala. 455; American Homestead Co. Ala. 455; American Homesteau Co. V. Linigan, 46 La. Ann. 1118; South Bay Meadow Dam Co. v. Gray, 30 Me. 547; Phoenix Warehousing Co. v. Badger, 6 Hun, 293, 67 N. Y. 294; Danbury & Norwalk R. Co. v. Wilson, 22 Conn. 435; Canfield v. Gregory, 66 Conn. 9; Litchfield Bank v. Church, 29 Conn. 137; Ohio & Mississippi R. Co. v. McPherson, 35 Mo. 13, 86 Am. Dec. 128; Smith v. Heidecker, 39 Mo. 157; Rutz v. Esler & Ropiequet Mfg. Co., 3 Ill. App. 83; Hickling v. Wilson, 104 Ill. 54; Dows v. Napier, 91 Ill. 44; Ramsey v. Peoria Marine & Fire Ins. Co., 55 Ill. 311; Corwith v. Culver, 69 Ill. 502; State Bank Building Co. v. Pierce, 92 Iowa, 668; Hager v. Cleveland, 36 Md. 476; Musgrave v. Morrison, 54 Md. 161; Macfarland v. West Side Improvement Ass'n, 53 Neb. 417; Bell's Appeal, 115 Pa. St. 88, 2 Am. St. Rep. 532; Weinman v. Wilkinsburg & East Liberty Passenger Ry. Co., 118 Pa. St. 192; Wadesboro Cotton Mills Co. v. Navigation Co. v. Neal, 3 Hawks Wash. 249.

(N. C.) 520; Marshall Foundry Co. v. Killian, 99 N. C. 501, 6 Am. St. Rep. 539; East Pascagoula Hotel Co. v. West, 13 La. Ann. 545; Aultman v. Waddle, 40 Kan. 195; Hunt v. Kansas & Missouri Bridge Co., 11 Kan. 412; Rockville & Washington Turnpike Road v. Van Ness, 2 Cranch, C. C. 449, Fed. Cas. No. 11, 986; Minnesota Gas-Light Economizer Co. v. Denslow, 46 Minn. 171; Ogden Clay Co. v. Harvey, 9 Utah, 497; Greenbrier Industrial Exposition v. Squires, 40 W. Va. 307; Black River Improvement Co. v. Holway, 85 Wis. 344; Thompson v. Reno Savings Bank, 19 Nev. 103, 3 Am. St. Rep. 797; Central Plank Road Co. v. Clemens, 16 Mo. 359; United Growers' Co. v. Eisner, 22 App. Div. (N. Y.) 1.

s20 Where a subscriber for stock in a corporation to be subsequently organized paid for one of his shares, and transferred others after an attempted organization, it was held that he could not deny the legal existence of the corporation. Bell's Appeal, 115 Pa. St. 88, 2 Am. St. Rep. 532. See, also, Maltby v. Northwestern Virginia R. Co., 16 Md. 422.

But a stockholder will not be estopped to deny the corporate existence by his payment of part assessments, unless they were called under color of corporate authority, and not as preliminary to organization. Schloss v. Montgomery Trade Co., 87 Ala. 414, 13 Am. St. Rep. 51. See, also, Birge v. Browning, 11 Wash. 249.

to deny that he is a subscriber and stockholder, or to allege that the subscription was invalid, not only as against creditors of the corporation, but also as against the corporation itself, or its assignee in bankruptcy or insolvency.821 Of course, if a

821 Sanger v. Upton, 91 U. S. 56; Newland Hotel Co. v. Wright, 73 Mo. App. 240; Erskine v. Loewen-stein, 82 Mo. 301, 11 Mo. App. 595; Clarke v. Thomas, 34 Ohio St. 46; Boggs v. Olcott, 40 Ill. 303; Lane v. Brainerd, 30 Conn. 565; Danbury & Norwalk R. Co. v. Wilson, 22 Conn. 435; Musgrave v. Morrison, 54 Md. 161; Nugent v. Supervisors of Putnam County, 19 Wall. (U. S.) 241; Thompson v. Reno Savings Bank, 19 Nev. 103, 3 Am. St. Rep. 797; Ross v. Bank of Gold Hill, 20 Nev. 191; Ruggles v. Brock, 6 Hun (N. Y.) 164; Clark v. Monongahela Navigation Co., 10 Watts (Pa.) 364; Erie & Waterford Plank Road Co. v. Brown, 25 Pa. St. 156; Barlow v. Wren, 1 Walk. (Pa.) 297; Greenville & Columbia R. Co. v. Coleman, 5 Rich. Law (S. C.) 118; Greenville & Columbia R. Co. v. Woodsides, 5 Rich. Law (S. C.) 145, 55 Am. Dec. 708; Portland & Fairview R. Co. v. Spillman, 23 Or. 587; Kampmann v. Tarver (Tex. Civ. App.) 29 S. W. 1144; McCormick v. Great Bend Gas & Fuel Co.. 48 Kan. 614; Tama Water-Power Co. v. Hopkins, 79 Iowa, 653; Canfield v. Gregory, 66 Conn. 9; Ex parte Besley, 2 Mac. & G. 176; Corwith v. Culver, 69 III. 502; Hickling v. Wilson, 104 Ill. 54; Blien v. Rand, 77 Minn. 110; Kansas City Hotel Co. v. Harris, 51 Mo. 464; Griswold v. Seligman, 72 Mo. 110; Beals v. Buffalo Expanded Metal Const. Co., 49 App. Div. (N. Y.) 589; Graff v. Pittsburgh & Steubenville R. Co., 31 Pa. St. 489; Pittsburgh, Wheeling & K. R. Co. v. Applegate, 21 W. Va. 172.

A subscriber cannot escape liability on his subscription by setting up his failure to sign the articles as required by statute, where he voted his stock at the preliminary meeting of the stockholders, authorizing nine of the stockhold-

ers to complete the organization of the corporation and sign as holders of all the stock. Newland Hotel Co. v. Wright, 73 Mo. App. 240.

A party who has permitted his name to remain in the certificate of incorporation as that of a subscriber for shares, and who has shared in the profits of the corporation, cannot afterwards deny the subscription, particularly as against creditors. Thompson v. Reno Savings Bank, 19 Nev. 103, 3 Am. St.

Rep. 797.

One who signs a subscription book for stock in a proposed corporation for the purpose of inducing others to subscribe, leaving the amount of his subscription blank, will be estopped, as against other subscribers and creditors, to deny the authority of the officers or agents of the corporation to fill in the blank. Jewell v. Rock River Paper Co., 101 Ill. 57.

A person who applies for and is allotted shares under an alias is estopped from denying his liability as a shareholder. In re Central Klondyke Gold Mining & Trading Co., 5 Manson, Bankr. Cas. 336.

Where a person represents or admits that he is a subscriber, and others subscribe on the faith of such representation or admission. he is estopped to deny that he is a subscriber, or that his subscription is binding. Groff v. Pittsburgh & Steubenville R. Co., 31 Pa. St.

A person who gives his note in payment of a subscription to the stock of a corporation is estopped to set up, to escape liability thereon, that the transaction was a fraud upon the cash subscribers. Clark v. Farrington, 11 Wis. 306. see ante, § 385.

A person who orally subscribes for stock, and recognizes the subscription as binding by postponing person has never subscribed for stock, and has never held or become entitled to any, he cannot be estopped to deny that he is a stockholder by the mere fact that his name appears as a subscriber on the corporate books.822

A subscriber is estopped, particularly as against creditors, to say that his subscription was fictitious, or was made fraudulently with a view to evading the requirements of the charter.<sup>823</sup>

A subscriber cannot allege that his subscription was not made in good faith, for the purpose of raising the point that the full amount of stock has not been subscribed, or for any other purpose.824

A subscriber who was also a commissioner to receive subscriptions for the purpose of organizing a corporation, and who has certified that the subscriptions have all been taken in good faith and in compliance with the law, is estopped to allege that his subscription was fraudulent or invalid or conditional.825

A subscriber for stock may be estopped by recitals in the articles of association or subscription book or paper which he

the time of payment until the corporation, on the faith of it, enters into contracts and makes improvements on its property, is estopped, in an action by the corporation, to deny the validity of the subscription on the ground that it was not in writing. Perkiomen Brick Co. v. Dyer, 187 Pa. St. 470.

Where subscribers have acted as stockholders for a number of years, they are estopped to set up the fact that they were not eligible for membership under articles of association limiting the membership to persons of a particular nationality. Blien v. Rand, 77 Minn. 110.

Where a subscriber votes at meetings or otherwise acts as a stockholder after organization, he cannot escape liability on his subscription by setting up that the corporation was formed for a different purpose or for a longer period than was provided for in his (Pa.) 269; Bavington v. Pittsburgh subscription. Greenbrier Industri- & Steubenville R. Co., 34 Pa. St. al Exposition v. Squires, 40 W. Va. 358.

307, 52 Am. St. Rep. 884; Nickum v. Burckhardt, 30 Or. 464, 60 Am. St. Rep. 822.

One who participates in the organization of a corporation cannot escape liability on his subscription on the ground that the purposes stated in the articles of incorporation differ from those stated in the original agreement for organization, or in the subscription. Nickum v. Burckhardt, 30 Or. 464, 60 Am. St. Rep. 822.

822 Lathrop v. Kneeland, 46 Barb, (N. Y.) 432.

823 Minor v. Mechanics' Bank of Alexandria, 1 Pet. (U.S.) 46; Graff v. Pittsburgh & Steubenville R. Co., 31 Pa. St. 489.

824 Bushnell v. Consolidated Ice-Machine Co., 138 Ill. 67, 1 Smith's Cas. 112.

825 Grayble v. York & Gettysburg Turnpike Road Co., 10 Serg. & R. has signed. As a general rule, if the articles of association or subscription paper contain recitals to the effect that certain requirements of the charter or enabling act have been complied with, all subscribers who sign the articles are estopped to deny the truth of such recitals for the purpose of avoiding liability on their subscriptions,826 unless the recitals are too ambiguous to operate as an estoppel,827 or the requirements of the charter or statute are such that they cannot be waived by the subscribers.828

Estoppel to set up release or discharge.—As we have seen in previous sections, a subscriber may, upon various grounds, be released or discharged from liability on his subscription. Thus, he may be discharged by an alteration of his subscription, by alteration or amendment of the charter of the corporation, by consolidation, by nonperformance of conditions precedent, He may, however, be estopped to set up a release or discharge, and as a general rule he will be estopped, both as against creditors of the corporation and as against the corporation itself, if with full knowledge of the facts he expressly waives the ground of discharge, or if he afterwards acts as a stockholder by taking part in meetings or otherwise.830

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827 Where articles of association stated that the capital stock had been bona fide subscribed, and "one-half thereof actually paid up," it was held that the statement was ambiguous as to whether one-half of the aggregate capital or of each share subscribed for had been paid, and did not estop a stockholder from showing the truth as to his subscription, and what had been actually paid thereon. Shepard v. Drake, 61 Mo. App. 134.

828 See New York & Oswego Midland R. Co. v. Van Horn, 57 N. Y.

826 Royce v. Tyler, 2 Ohio Cir. Ct. nellsville R. Co., 32 Pa. St. 25; Pittsburgh & Connellsville R. Co. v. Stewart, 41 Pa. St. 54.

830 Tama Water-Power Co. v. Hopkins, 79 Iowa, 653; Detroit Driving Club v. Fitzgerald, 109 Mich. 670; Chetlain v. Republic Life Ins. Co., 86 Ill. 220; Canfield v. Gregory, 66 Conn. 9: Kennebec & Portland R. Co. v. Palmer, 34 Me. 366: Duluth Investment Co. v. Witt, 63 Minn. 538; Kirkwood Gymnasium & Armory Hall Ass'n v. Van Ness, 61 Mo. App. 361; Barlow v. Wren, 1 Walk. (Pa.) 297; Gibbons v. Ellis, 83 Wis. 434.

A person who subscribes for stock in a corporation to be formed, and who afterwards pays part of his subscription, votes at elec-829 See ante, § 474 et seq. Com-pare McCully v. Pittsburgh & Con-estopped, in a suit to recover the course, there must have been knowledge of the facts, actual or constructive, in order that his continuing as a stockholder may estop him.831

Estoppel to set up nonperformance of conditions precedent.-A subscriber may be estopped by his conduct from setting up as a defense, to defeat an action on his subscription, that express or implied conditions precedent upon which the subscription was made have not been performed. It is a general rule that when a subscription is upon a condition precedent, express or implied, the subscriber is estopped to set up nonperformance of the condition, if, with knowledge that it was not performed, he has participated in stockholders' meetings, and in voting for expending money or making contracts, or in any other acts which could not be properly done except upon the assumption that performance of the condition was waived.832 For example, a subscriber may be so estopped from setting up nonperformance of an express or implied condition that the whole amount of the capital stock, or a certain percentage thereof, should be subscribed.833 And a subscriber may be estopped to set up his failure to pay a certain percentage of his subscription at the time of subscribing, as required by the charter or enabling The same is true of any other condition precedent, unless it is one which is imposed by the legislature, and which the subscribers cannot waive.835

Estoppel to set up conditional delivery of subscription.—A subscriber will be estopped to set up that his subscription was delivered to the promoter of the corporation subject to an oral

balance of his subscription, to set Am. Dec. 300; Hager v. Cleveland, up that the corporation as organized is of a different nature from the one contemplated when he subscribed. Barlow v. Wren, 1 Walk. (Pa.) 297.

831 Strong v. Southwestern Bridge & Iron Co. (Tex. Civ. App.) 38 S. W. 546; Denny Hotel Co. v. Gilmore, 6 Wash. 152.

832 New Hampshire Central R. Co. v. Johnson, 30 N. H. 390, 64

36 Md. 476; Canfield v. Gregory, 66 Conn. 9; Duluth Investment Co. v. Witt, 63 Minn. 538; International Fair & Exposition Ass'n v. Walker, 97 Mich. 159; Detroit Driving Club v. Fitzgerald, 109 Mich. 670. And see ante, § 463.

833 See ante, § 507.

834 Ante. § 510.

835 See ante, § 463.

condition, where others have subscribed and made payments, and the corporation has been formed, and has expended money and contracted liabilities, all on the faith of the subscriptions, and in ignorance of the oral condition.<sup>836</sup>

Estoppel of corporation and other subscribers.—Estoppel to deny the validity of a subscription does not operate against the particular subscriber only. The corporation and the other subscribers may also be estopped. If a corporation accepts a subscription which is not made with the formalities prescribed by the charter, enabling act, or articles of association, and the other stockholders consent or acquiesce, both the corporation and the other stockholders will be estopped to deny that the subscription is valid, unless the provisions of the charter or enabling act are such as to render it absolutely void.<sup>837</sup>

sse Minneapolis Threshing Machine Co. v. Davis, 40 Minn. 110, 12 168 Pa. St. 30. Compare Coyote Am. St. Rep. 701. See ante, § 464. Gold & Silver Mining Co. v. Ruble, 8 Or. 284.

### CHAPTER XXII.

#### MISCELLANEOUS RIGHTS OF STOCKHOLDERS.

- I. RIGHT TO DIVIDENDS.
  - § 516. Definition and nature of dividends.
    - 517. Stockholders' right to share in profits.
    - 518. Right of corporations to pay dividends-In general.
    - 519. Dividends payable out of profits only.
    - Determination of profits for the purpose of declaring dividends.
    - 521. Interest and interest dividends.
    - 522. Set-off of dividends against debts due from stockholders.
    - 523. Mode of declaring and paying dividends.
    - 524. Time of payment of dividends.
    - 525. Persons who are entitled to dividends.
    - 526. Rights of persons entitled to the income and profits of shares.
    - 527. Remedies of stockholders to recover dividends.
    - 528. Remedies in case of unlawful payment of dividends.
    - 529. Rights of preferred stockholders.
- II. RIGHT TO INSPECT BOOKS AND PAPERS OF THE CORPORATION.
  - § 530. In general.
    - 531. Express provisions in the charter, general law, articles of association, or by-laws.
    - 532. Examination by attorney or agent.
    - 533. Remedy of stockholders on denial of right.
- III. CONTRACTS AND CONVEYANCES BETWEEN A CORPORATION AND ITS STOCKHOLDERS.
  - § 534. In general.
- IV. ACTIONS BY STOCKHOLDERS TO ENFORCE INDIVIDUAL RIGHTS, OR REDRESS OR PREVENT INDIVIDUAL INJURIES.
  - § 535. In general.
  - V. REMEDIES OF STOCKHOLDERS FOR INJURIES TO THE CORPORATION.
    - § 536. In general.

- 537. Actions at law to redress injuries to the corporation.
- 538. The general right of stockholders to sue in equity.
- 539. Suits to enjoin or set aside ultra vires transactions, and prevent or redress diversion of assets.
- 540. Suits for redress or relief in case of fraud of the majority of stockholders.
- 541. Suits for redress or relief in case of fraud, excess of authority, or negligence of directors or other officers.
- 542. Suits against third persons to enjoin or redress injuries to the corporation.
- 543. Necessity for effort to obtain relief through the corporation or its officers.
- 544. Discretionary powers of the directors or majority of the stockholders.
- 545. Summary of circumstances necessary to enable the stockholder to sue.
- 546. Defense by stockholder in suits against the corporation.
- 547. Suit or defense by stockholder in the name of or for the corporation.
- 548. Effect of assignment by the corporation.
- 549. Effect of dissolution of the corporation.
- 550. Suits by stockholders in the federal courts.
- 551. Persons entitled to sue as stockholders.
- 552. Motive of stockholder-Extent of interest.
- 553. Laches and estoppel.
- 554. Parties to stockholders' suits.
- 555. Judgment or decree as a bar.
- 556. Appointment of receiver-Winding up or dissolution.

#### I. RIGHT TO DIVIDENDS.

§ 516. Definition and nature of dividends. A dividend is a fund set apart out of the profits of a corporation for distribution among its stockholders or members in proportion to their respective shares or interest in the corporation.

The object of modern business corporations is to earn money for their stockholders or members. When such a corporation earns profits over and above the amount of its capital, the stockholders or members have the right, subject to qualifications which will be shown in the following sections, to have such profits set apart from the general mass of the funds of the corporation, and distributed among them in proportion to their shares or interest in the corporation, and the fund set apart for

this purpose is called a "dividend." The term is also used to designate the shares of the individual stockholders or members in the fund so set apart.

To declare a dividend is to announce a readiness to pay a specified dividend.

To make a dividend is to actually set apart a sum to be divided as explained above.

To pass a dividend is to omit to make a regular or expected dividend.

A stock dividend is a division of profits, actual or anticipated, payable in reserved or additional stock, instead of cash.<sup>2</sup>

A cumulative dividend is a dividend with regard to which it is agreed that, if at any time it is not paid in full, the difference shall be added to the payment following. Thus, if a cumulative dividend is six per cent. on the capital stock, and only five per cent. is paid, the amount due at the next payment will be seven per cent.3

The expressions "dividend on" and "dividend off" are stockexchange phrases, meaning that, on the day of closing the transfer books of any stock for a dividend, the transactions in such

11 Morawetz, Corp. § 435; Hyatt holders." City of Allegheny v. v. Allen, 56 N. Y. 553, 15 Am. Rep. Pittsburgh, Allegheny & M. P. R. 449; Lockhart v. Van Alstyne, 31 Co., 179 Pa. St. 414.

Mich. 76, 18 Am. Rep. 156, 2 Keener's Cas. 1354.

The term "dividend" is also used to designate the assets distributed

"The term 'dividend' in its technical as well as in its ordinary acceptation means that portion of its profits which the corporation, by its directory, sets apart for ratable division among its shareholders." Mobile & Ohio R. Co. v. Tennessee, 153 U. S. 486, 2 Keener's Cas. 1295.

"A dividend is 'the share of a sum divided that falls to each individual, a distributive sum, share or percentage, applied to the profits as apportioned among stockhold-It differs from profits in being taken by competent authority out of the joint property of the partnership or company, and transferred to the separate property of the individual partners or stock-

by a corporation among its stockholders out of capital, on reduction of the capital stock or dissolution. Larwill v. Burke, 19 Ohio Cir. Ct. R. 513.

As to what constitutes the declaration of a dividend for the purposes of taxation, see ante, § 286(d), and cases there collected.

A sale of the bulk of the property of a corporation, evidenced by a transfer of shares, the proceeds being distributed among the stockholders, is not a distribution of a dividend, but a sale of shares. Rorke v. Thomas, 56 N. Y. 559.

- <sup>2</sup> Post, § 523(e).
- 3 Post, § 529(d).

stock for cash include, or do not include, the dividend up to the time officially designated for closing the books.

"Dividends" and "profits" distinguished.—The profits of a corporation in its hands do not become a "dividend" until they have been set apart, or at least declared, as a dividend. Therefore a reservation of "all dividends" by a stockholder on selling his stock does not include profits which have been made by the corporation, where no dividend has been declared.

Power to declare dividend.—Every private corporation, whether it has a capital stock or not, has the inherent power to declare dividends when it has undivided profits. Mutual insurance companies, for example, although they have no capital stock, have the right to declare dividends when they have accumulated a surplus.<sup>5</sup>

The power to declare dividends is vested, in the absence of express provision to the contrary, not in the stockholders, in the board of directors.

§ 517. Stockholders' right to share in profits—(a) In general.—Until a dividend has been fully declared, the stockholders of a corporation have no legal right or title to any part of the assets of the corporation, although the assets may consist in part of surplus profits out of which a dividend might properly be declared; but as soon as the directors have properly declared a dividend, each stockholder acquires a legal right to his share, and may maintain an action against the corporation to recover the same.

It follows that, after a dividend has been lawfully declared by the directors, and the right of the stockholders to their shares has r/vested, the action of the directors cannot be revoked.

Nor are the rights of stockholders as creditors of the corporation affected by its subsequent insolvency.

It is discretionary with the directors of a corporation whether they will declare a dividend, even when there are surplus profits, and, as a general rule, the courts will not control them in the ex-

<sup>4</sup> Hyatt v. Allen, 56 N. Y. 553, 15 5 McKean v. Biddle, 181 Pa. St. Am. Rep. 449. And see post, § 519. 361. 6 See post, chapter xxiv.

ercise of this discretion, unless they act in bad faith or unreasonably.

- (b) Rights before dividend is declared.—As was shown in a previous chapter, the property of a corporation belongs in law to the corporation, and not to the stockholders. This is just as true of the profits earned by a corporation as it is of its other assets. The stockholders of a corporation may have the equitable right to insist that the profits from the corporate business shall be divided among them, but they have no legal right to any share therein, nor is there any indebtedness to them on the part of the corporation, so as to entitle them to maintain an action against it, until a dividend has been made or declared; and it can make no difference that the amount of the profits and the condition of the corporation are such that the directors might or should declare a dividend, and would be compelled by a court of equity to do so.
- (c) Rights after a dividend is declared.—After a dividend has been set apart or declared, the rule is different. As soon as a dividend is lawfully and fully declared out of surplus profits, the corporation becomes indebted from that moment to each

Am. Dec. 758; Curry v. Woodward, 44 Ala. 305; Jackson's Adm'r v. Newark Plankroad Co., 31 N. J. Law, 277, 2 Keener's Cas. 1418, 2 Cum. Cas. 201; Waterman v. Alden, 42 Ill. App. 294; Minot v. Paine, 99 Mass. 101, 96 Am. Dec. 705; Wheeler v. Northwestern Sleigh Co., 39 Fed. 347, 2 Cum. Cas. 203; Burroughs v. North Carolina R. Co., 67 N. C. 376, 12 Am. Rep. 611; State v. Baltimore & Ohio R. Co., 6 Gill (Md.) 363; Gibbons v. Mahon, 136 U. S. 549.

Van Alstyne, 31 Mich. 76, 18 Am. Rep. 156, 2 Keener's Cas. 1354; to receive all dividends on stock Williston v. Michigan Southern & so long as he remains in a certain Northern Indiana R. Co., 13 Allen employment, and he quits before (Mass.) 400; Spooner v. Phillips, 62 Conn. 62; Hill v. Atoka Coal & entitled to any dividends there-Mining Co. (Mo.) 21 S. W. 508; after declared. Clapp v. Astor, 2 Goodwin v. Hardy, 57 Me. 143, 99 Edw. Ch. (N. Y.) 379.

<sup>7</sup> Ante, § 6(c).

<sup>8</sup> Post, §§ 517(f), 527(b).

<sup>9</sup> Phelps v. Farmers' & Mechanics' Bank, 26 Conn. 269; Hyatt v. Allen, 56 N. Y. 553, 15 Am. Rep. 449; Beveridge v. New York Elevated R. Co., 112 N. Y. 1; Boardman v. Lake Shore & Michigan Southern Ry. Co., 84 N. Y. 157, 2 Keener's Cas. 1368; Jermain v. Lake Shore & Michigan Southern Ry. Co., 91 N. Y. 483, 2 Keener's Cas. 1411; Scott v. Eagle Fire Co., 7 Paige (N. Y.) 198; Lockhart v. Van Alstyne, 31 Mich. 76, 18 Am. Rep. 156, 2 Keener's Cas. 1354; Williston v. Michigan Southern & Northern Indiana R. Co., 13 Allen (Mass.) 400; Spooner v. Phillips, 62 Conn. 62; Hill v. Atoka Coal & Mining Co. (Mo.) 21 S. W. 508; Goodwin v. Hardy, 57 Me. 143, 99

stockholder for the amount of his share, and he may recover the same in an action against the corporation.<sup>10</sup>

When the directors of a corporation have merely declared a dividend, the corporation becomes a mere debtor to each stockholder for the amount due him, and the stockholders are in the same position as other creditors. There is no trust relation, but simply the relation of debtor and creditor. And this is true, notwithstanding the corporation may have an account with each stockholder on its books, and may credit him with the amount of the dividend due him. But when the directors have not only declared a dividend, but have set apart and appropriated a fund for the payment thereof, the fund so set apart and appropriated is thereby separated from the other assets of the corporation, and becomes a trust fund in the hands of the corporation, and the stockholders have a right to insist that it shall be applied in payment of the dividend, to the exclusion of any other claim against the corporation.

10 Ford v. Easthampton Rubber Thread Co., 158 Mass. 84, 35 Am. St. Rep. 462, 1 Smith's Cas. 329, 2 Keener's Cas. 1338; Beers v. Bridgeport Spring Co., 42 Conn. 17, 2 Keener's Cas. 1429; Le Roy v. Globe Ins. Co., 2 Edw. Ch. (N. Y.) 657, 1 Smith's Cas. 325, 2 Keener's Cas. 1327; In re Le Blanc, 14 Hun (N. Y.) 8, 75 N. Y. 598; King v. Paterson & Hudson River R. Co., 29 N. J. Law, 82, 2 Keener's Cas. 1330; University v. North Carolina R. Co., 76 N. C. 103, 22 Am. Rep. 671; Wheeler v. Northwestern Sleigh Co., 39 Fed. 347, 2 Cum. Cas. 203; Jackson's Adm'r v. Newark Plankroad Co., 31 N. J. Law, 277, 2 Keener's Cas. 1418, 2 Cum. Cas. 201; West Chester & Philadelphia R. Co. v. Jackson, 77 Pa. St. 321.

Where a stockholder accepts payment of a dividend, which is stated by the resolution declaring the same to be in lieu of a dividend previously declared, with knowledge of the resolution, he is estopped to claim payment of the 8,75 N. Y. 598.

ridend first declared. Albany Fertilizer & Farm Improvement Co. v. Arnold, 103 Ga. 145.

1581

A by-law declaring a certain per cent. dividend on preferred stock from net earnings at an annual date, the remaining net profits, if any, to be devoted to a dividend on common stock, is in effect an appropriation of the net earnings to dividends, and has the force and effect of a contract. Seattle Trust Co. v. Pitner, 18 Wash. 401.

11 In re Severn & Wye & Severn Bridge Ry. Co., 74 Law T. (N. S.) 219, 1 Smith's Cas. 322, 2 Keener's Cas. 1342. And see Hunt v. O'Shea, 69 N. H. 600.

12 In re Severn & Wye & Severn Bridge Ry. Co., 74 Law T. (N. S.) 219, 1 Smith's Cas. 322, 2 Keener's Cas. 1342.

13 Le Roy v. Globe Ins. Co., 2 Edw. Ch. (N. Y.) 657, 1 Smith's Cas. 325, 2 Keener's Cas. 1327. And see In re Le Blanc, 14 Hun (N. Y.) 8, 75 N. Y. 598.

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- (d) Revocation of declaration of dividend.—Since the right of the stockholders of a corporation to a dividend becomes vested as soon as the dividend has been fully declared by the directors, and the corporation becomes their debtor for their respective shares, it necessarily follows that neither the same board of directors nor their successors can afterwards reconsider their action and revoke the declaration without the stockholders' consent.14 It has been held, however, that a mere vote of the directors to pay a dividend may be revoked, either by them or by their successors, if it has not been made public, or communicated to the stockholders, and no fund has been set apart or appropriated for payment of the dividend, since, until there has been at least a communication of the vote, the action of the directors is not final.15
- (e) Effect of insolvency.—Since the stockholders of a corporation have no legal right to share in its profits until a dividend has been declared, the right of creditors of an insolvent corporation to have its assets applied to the satisfaction of their claims, before any distribution among the stockholders, attaches, not only to the capital of the corporation, but also to undivided profits out of which a dividend might have been declared if the corporation had not become insolvent.<sup>16</sup> But when a dividend has been fully and lawfully declared, the stockholders are in precisely the same position as other creditors. If the corporation becomes insolvent before the dividend is paid or set apart, they are entitled to share pro rat creditors:17 and if it becomes insolvent after the dividend is

Co., 42 Conn. 17, 2 Keener's Cas. 1429; King v. Paterson & Hudson River R. Co., 29 N. J. Law, 82, 2 Schlichter Jute Cordage Co., 167 Pa. St. 370. See, also, Terry v. Eagle Lock Co., 47 Conn. 141. And see the other cases cited in the notes

It has been held, however, that a declaration of a stock dividend by the stockholders of a corporation does not give a stockholder a vest-

14 See Beers v. Bridgeport Spring ed interest in the stock, so as to Co., 42 Conn. 17, 2 Keener's Cas. prevent a subsequent vote rescind-1429; King v. Paterson & Hudson ing the declaration. Terry v. Eagle River R. Co., 29 N. J. Law, 82, 2 Lock Co., 47 Conn. 141. But see Keener's Cas. 1330; Dock v. Dock v. Schlichter Jute Cordage Co., 167 Pa. St. 370.

15 Ford v. Easthampton Rubber Thread Co., 158 Mass. 84, 35 Am. St. Rep. 462, 1 Smith's Cas. 329, 2 Keener's Cas. 1338.

16 Scott v. Eagle Fire Co., 7 Paige (N. Y.) 198; Curry v. Woodward, 44 Ala. 305.

17 See note 20, infra.

paid, they cannot be made to refund for the benefit of creditors.18

When dividends have not only been declared out of surplus profits, but the fund for their payment has been set apart, and distinguished from the general mass of the company's funds, the fund so set apart becomes a trust fund for the payment of the dividends, and the right of the stockholders to receive the same as against creditors of the corporation is not affected by the subsequent insolvency of the corporation.<sup>19</sup> This principle does not apply where the funds are not set apart and appropriated to the payment of a dividend which has been declared. And it has been held that merely crediting each stockholder with the amount due him on the books of the corporation is not such a setting apart of the fund as to make the corporation a trustee instead of a mere debtor to the stockholders.<sup>20</sup>

(f) Compelling declaration and payment of dividends.-If the directors of a corporation abuse their discretion, and fraudulently or arbitrarily refuse to pay a dividend, when the condition of the corporation makes it their duty to do so, a court of equity will compel them to do so at the suit of a stockholder.21

19 Le Roy v. Globe Ins. Co., 2 Edw. Ch. (N. Y.) 657, 1 Smith's Cas. 325, 2 Keener's Cas. 1327.

In this case, the board of directors of an insurance company declared a dividend at a time when there were surplus profits out of which it was proper to pay a dividend, fixed the day for its payment. published the fact in the newspa-pers, carried the amount on its books to the debit of profit and loss, and apportioned the same among the stockholders by filling up and signing checks upon the bank in which the funds were deposited for the purpose of delivery to each stockholder when called for. Afterwards there was a dis-

18 Stringer's Case (In re Mercanhands of a receiver. It was held tile Trading Co.), L. R. 4 Ch. App. that the fund was so set apart by 475, 1 Smith's Cas. 334, 2 Keener's the company, and distinguished from the general mass of its funds, that it became a trust fund for the payment of the dividends, and that the stockholders were entitled the stockholders were entitled thereto. See, also, In re Le Blanc, 14 Hun (N. Y.) 8, 75 N. Y. 598; Van Dyck v. McQuade, 86 N. Y. 38; Peckham v. Van Wagenen, 83 N. Y. 40.

20 See In re Severn & Wye & Severn Bridge Ry. Co., 74 Law T. (N. S.) 219, 1 Smith's Cas. 322, 2 Keener's Cas. 1342; Curry v. Woodward, 44 Ala. 305; Lowne v. American Fire Ins. Co., 6 Paige (N. Y.) 482. But compare the cases cited in the note preceding.

 21 Pratt v. Pratt, Read & Co., 33
 Conn. 446, 2 Keener's Cas. 1421, 2 for. Afterwards there was a discum. Cas. 219; Beers v. Bridge-astrous fire, and the company beport Spring Co., 42 Conn. 17, 2 came insolvent and went into the Keener's Cas. 1429; Belfast & But it is a well-settled principle that whether or not dividends shall be paid, and the amount of the dividend at any time, is primarily to be determined by the directors, and there must be bad faith or a clear abuse of discretion on their part to justify a court of equity in interfering.<sup>22</sup>

79 Me. 411, 1 Am. St. Rep. 330; Scott v. Eagle Fire Co., 7 Paige (N. Y.) 198; Hiscock v. Lacy, 9 Misc. Rep. (N. Y.) 578; Laurel Springs Land Co. v. Fougeray, 50 N. J. Eq. 756, reversing Fougeray v. Cord, 50 N. J. Eq. 185, 2 Cum. Cas. 241; Rex v. Bank of England, 2 Barn. & Ald. 620, 2 Keener's Cas. 1416, 2 Cum. Cas. 218; Storrow v. Texas Consolidated Compress & Mfg. Ass'n (C. C. A.) 87 Fed. 612. See, also, Barnard v. Vermont & Massachusetts R. Co., 7 Allen (Mass.) 512; Earle v. Burland, 27 Ont. App. 540.

In New Jersey, a statute expressly makes it the duty of the directors of a corporation to declare regular dividends of its accumulated profits, if any exist after reserving, over and above its capital, such sum as working capital as may be fixed by the stockholders. And a stockholder may enforce this duty by a suit in equity. Griffing v. A. A. Griffing Iron Co.' (N. J. Ch.) 48 Atl. 910; Trimble v. American Sugar-Refining Co. (N. J. Ch.) 48 Atl. 912.

Under a statute requiring directors of corporations to declare regular dividends of their accumulated profits, if any exist after reserving, over and above their capital. such sum as working capital as may be fixed by the stockholders, a bill filed by a stockholder to compel declaration of a dividend is not demurrable, where it alleges that there are accumulated profits not reserved for working capital under the statute. Griffing v. A. A. Griffing Iron Co. (N. J. Ch.) 48

Moosehead Lake R. Co. v. City of ing that the corporation also has a Belfast, 77 Me. 445; Hazeltine v. large accumulation of profits which Belfast & Moosehead Lake R. Co., should be distributed as dividends, but not stating that such accumulation is larger than the stockholders have fixed as a reserve, is insufficient, for it will be presumed that such sum has been reserved by the stockholders as working capital. Trimble v. American Su-gar-Refining Co. (N. J. Ch.) 48 Atl. 912.

22 McNab v. McNab & Harlin Mfg. Co., 62 Hun (N. Y.) 18, 1 Smith's Cas. 332, 133 N. Y. 687; Burden v. Burden, 159 N. Y. 287, affirming 8 App. Div. 160; Morey v. Fish Bros. Wagon Co., 108 Wis. 520; New York, Lake Erie & W. R. Co. v. Nickals, 119 U. S. 296, 2 Keeper's Co. Cum. Cas. 228; Gibbons v. Mahon, 136 U. S. 549; State v. Bank of Louisiana, 6 La. 745; Pratt v. Pratt. Read & Co., 33 Conn. 446, 2 Keener's Cas. 1421, 2 Cum. Cas. 219: Phelps v. Farmers' & Mechanics' Bank, 26 Conn. 269; Jackson's Adm'r v. Newark Plankroad Co., 31 N. J. Law, 277, 2 Keener's Cas. 1418, 2 Cum. Cas. 201; Field v. Lamson & Goodnow Mfg. Co., 162 Mass. 388; Fougeray v. Cord, 50 N. J. Eq. 185, 2 Cum. Cas. 241, reversed in Laurel Springs Land Co. v. ed in Laurel Springs Land Co. v. Fougeray, 50 N. J. Eq. 756; Williams v. Western Union Telegraph Co., 93 N. Y. 162, 2 Keener's Cas. 1310, 2 Cum. Cas. 209; Beveridge v. New York Elevated R. Co., 112 N. Y. 1; Ely v. Sprague, 1 Clarke, Ch. (N. Y.) 351; Karnes v. Rochester & Genesee Valley R. Co., 4 Abb. Pr. (N. S.; N. Y.) 107; Belfast & Moosehead Lake R. Co. v. City of Belfast. 77 Me. 445; Hunter v. Griffing Iron Co. (N. J. Ch.) 48 Belfast, 77 Me. 445; Hunter v. Atl. 910.

But a bill alleging payment of a large dividend, and further alleg- Ala. 503; Wolfe v. Underwood, 96

The mere fact that a corporation has surplus profits out of which a dividend might lawfully be declared is not of itself sufficient ground for a court of equity to compel the directors to make a dividend, for they have a right to use surplus profits to extend the business of the corporation, or to make improvements, and even to provide a surplus fund, if it is to the interests of the corporation to do so, and a court of equity will not interfere with or control their discretion in determining what the interests of the corporation require in this respect, unless there is a clear abuse of discretion.<sup>23</sup> "When a corporation has a surplus," it was said in a New York case, "whether a dividend shall be made, and if made, how much it shall be, and when and where it shall be payable, rest in the fair and honest discretion. of the directors uncontrollable by the courts."24 In another case it was said: "The trustees are chosen by the shareholders, to exercise their best judgment, depending upon their knowledge of the affairs and condition of the company, and when that has been done, the courts do not undertake to control their action, although they might differ in their views of the proper management to be adopted and followed."25 There have been many other statements to the same effect.<sup>26</sup>

R. Co., 6 Gill (Md.) 363; Zellerbach v. Allenberg, 99 Cal. 57; McLean v. Pittsburgh Plate Glass Co., 159 Pa. St. 112.

St. 112.

<sup>23</sup> McNab v. McNab & Harlin
Mfg. Co., 62 Hun (N. Y.) 18, 1
Smith's Cas. 332, 133 N. Y. 687;
Burden v. Burden, 159 N. Y. 287,
affirming 8 App. Div. 160; Morey
v. Fish Bros. Wagon Co., 108 Wis.
520; Hunter v. Roberts, Throp &
Co., 83 Mich. 63; Earle v. Burland,
27 Ont. App. 540; Reynolds v. Bank
of Mt. Vernon, 6 App. Div. (N. Y.)
62, 158 N. Y. 740; and other cases
cited above. cited above.

But they cannot act unreasonably and oppressively. Where an ordinary trading company sets apart from profits a reserve fund far exceeding the amount necessary for that purpose, and particu-

Ala. 329; State v. Baltimore & Ohio larly when it has invested the same in unauthorized and hazardous investments, a court of equity, at the instance of minority stockholders, will order a distribution among stockholders of all except a reasonable reserve fund. Earle v. Burland, 27 Ont. App. 540. And see the other cases cited in note 21. supra.

> In New Jersey, a statute expressly allows corporations to reserve, over and above their capital, such sum as a working capital as may be fixed by the stockholders. See Griffing v. A. A. Griffing Iron Co. (N. J. Ch.) 48 Atl. 910; Trimble v. American Sugar-Refining Co. (N. J. Ch.) 48 Atl. 912.

<sup>24</sup> Williams v. Western Union Telegraph Co., 93 N. Y. 162, 2 Keen-er's Cas. 1310, 2 Cum. Cas. 209.

25 McNab v. McNab & Harlin

This is true, even though there may be an express provision in the charter of the corporation or the certificate of stock that dividends shall be paid each year out of the net profits of the company. In the supreme court of the United States it was said by Mr. Justice Harlan, speaking of a railroad company: "The directors of such corporations, having opportunities not ordinarily possessed by others of knowing the resources and condition of the property under their control, are in a better position than stockholders to determine whether, in view of the duties which the corporation owes to the public, and of all its liabilities, it will be prudent, in any particular year to declare a dividend upon stock. While their authority in respect of these matters may, of course, be controlled or modified by the company's charter, and while the power of the courts may be invoked for the protection of stockholders against bad faith upon the part of the directors, we should hesitate to assume that either the legislature or the parties intended to deprive the corporation, by its managers, of the power to protect the interests of all, including the public, by using earnings when necessary, or when, in good faith, believed to be necessary, for the preservation or improvement of the property intrusted to its control."27

Right of corporations to pay dividends-In general.-By express statutory provision in many states, and even in the absence of any statute, a corporation cannot lawfully reduce its capital stock by distributing any part thereof among the stockholders as dividends. The right to pay dividends is restricted to the net or

of the directors of a corporation are without limitation, and free from restraint, they are at liberty to exercise a very liberal discretion as to what disposition shall be made of the gains of the business of the corporation. Their power over them is absolute so long as they act in the exercise of an hon-

Mfg. Co., 62 Hun (N. Y.) 18, 1 Smith's Cas. 332, 133 N. Y. 687. 26 It was said in a New Jersey case: "In cases where the power for repairs and improvements, and to meet contingencies, both present and prospective." Park v. Grant Locomotive Works, 40 N. J. Eq. 114.

> 27 New York, Lake Erie & W. R. Co. v. Nickals, 119 U. S. 296, 2 Keener's Cas. 1399, 2 Cum. Cas. 228.

surplus profits,—the assets which remain after deducting the amount of the capital stock and all losses sustained and expenses incurred in conducting the business.

## § 519. Dividends payable out of profits only.

It is a well-settled principle that, as between the stockholders of a corporation and its creditors, the assets of the corporation are, in a sense, a trust fund for the payment of its debts, and they cannot lawfully be distributed among the stockholders, even in part, to the prejudice of creditors. Furthermore, the amount of the capital stock of corporations is very generally fixed by their charters or by a general law, and both the state and each stockholder of the corporation, as well as its creditors, have the right to insist that it shall not be reduced or impaired by any distribution among the stockholders. It is a settled rule, therefore, even in the absence of any statutory provision, that a corporation cannot lawfully declare dividends out of its capital stock, and thereby reduce the same, or out of assets which are. needed to pay the corporate debts. They can be declared only out of surplus profits.28

28 Birch v. Cropper, 14 App. Cas. 525; Wood v. Dummer, 3 Mason, 308, Fed. Cas. No. 17,944, 2 Keener's Cas. 1858, 1 Cum. Cas. 805; Warren v. King, 108 U. S. 389; Main v. Mills, 6 Biss. 98, Fed Cas. No. 8,974; Reid v. Eatonton Mfg. Co., 40 Ga. 98, 2 Am. Rep. 563; Taft v. Hartford, Providence & F. R. Co., 8 R. I. 310, 5 Am. Rep. 575, 1 Smith's Cas. 347; Hubbard v. Weare, 79 Iowa, 678; Williams v. Boice, 38 N. J. Eq. 364, 1 Smith's Cas. 339; Lockhart v. Van Alstyne, 31 Mich. 76, 18 Am. Rep. 156, 2 Keener's Cas. 1354; Chaffee v. Rut-land R. Co., 55 Vt. 110; Hughes v. Cas. 305, Lockhart v. van Alstyne, quent years in which no profits 31 Mich. 76, 18 Am. Rep. 156, 2 are made. Mills v. Northern Ry. Keener's Cas. 1354; Chaffee v. Rutland R. Co., 55 Vt. 110; Hughes v. 621, 1 Smith's Cas. 352; Hoole v. Vermont Copper Mining Co., 72 N. Great Western Ry. Co., 3 Ch. App. Y. 207; Miller v. Ratterman, 47 Chio St. 141; Martin v. Zellerbach, 38 Cal. 300, 99 Am. Dec. 365; American Wire Nail Co. v. Gedge, 96 Ky. 513; Citizens' Nat. Bank v. Drouillard, 6 Ky. Law Rep. 588; Field v. Keener's Cas. 1429.

Lamson & Goodnow Mfg. Co., 162 Mass. 388; Slayden v. H. J. Seip Coal Co., 25 Mo. App. 439; In re National Funds Assurance Co., 10 Ch. Div. 118; Leary v. Columbia River & Puget Sound Navigation Co., 82 Fed. 775; Grant v. Southern Contract Co. (Ky.) 47 S. W. 1091. This is true of ordinary preferred stock. See post, § 529(c).

Profits which have been made and allowed to accumulate may be paid out as dividends in subsequent years in which no profits

In many jurisdictions this rule has, in somewhat varying language, been expressly declared by statute, and in some jurisdictions a penalty is imposed upon officers of a corporation who shall violate the statute. Thus, in New York it is provided by statute that the directors or managers of a corporation shall make no dividend except from surplus profits, and that they shall not divide, withdraw, or in any manner pay to the stockholders any portion of the capital stock of the corporation. And the Penal Code makes a violation of the statute a misdemeanor.

Unconditional agreement to pay dividend.—From the rule that dividends can only be paid out of surplus profits, it follows that a corporation has no power to enter into an unconditional agreement to pay dividends to shareholders, without regard to the condition of the corporation at the time of payment. Such an agreement is ultra vires and void.29

#### § 520. Determination of profits for the purpose of declaring dividends.

(a) In general.—It is clear that there cannot be surplus or net profits for the purpose of declaring a dividend, unless the total value of the assets of the corporation at the time it is proposed to declare the dividend exceeds the amount of its capital stock, after deducting all expenses which have been incurred. and all losses which have been sustained. It may be laid down as a general proposition, therefore, subject to the qualifications shown in the following sections, that the surplus or net profits of a corporation are the difference between the total present value of its assets, after deducting losses and liabilities, and the amount of its capital stock.30 In a New York case it was said:

<sup>29</sup> Guinness v. Land Corporation is void under a constitutional pro-4 Am. St. Rep. 798.

A contract by which a corporation agrees to repay to a purchaser ery Ass'n, 123 Ala. 538.

of stock in dividends an amount equal to the amount paid therefor Works, 40 N. J. Eq. 114; Main v.

of Ireland, 22 Ch. Div. 349, 2 Keen- vision that no corporation shall isof Irefand, 22 Ch. biv. 347, 2 Keenvision that no corporation shall is
er's Cas. 1286; Memphis Grain & sue stock except for money, labor
Package Elevator Co. v. Memphis done, or money or property actu& Charleston R. Co., 85 Tenn. 703, ally received, and all fictitious issues of stock shall be void. Smith

"The capital stock of a corporation, is, like that of a co-partner-ship or joint stock company, the amount which the partners or associates put in as their stake in the concern. To this they add upon the credit of the company, from the means and resources of others, to such extent as their own prudence or the confidence of such other persons will permit. Such additions create a debt; they do not form capital. And if successful in their career, the surplus over and above their capital and debts becomes profits, and is either divided among the partners and associates, or used still further to extend their operations."<sup>31</sup>

The mere fact that a corporation is indebted does not prevent it from paying a dividend, if the fair value of its assets exceeds its indebtedness as well as its capital stock to the extent of the dividend declared.<sup>32</sup>

(b) Property or money representing capital stock.—Property or money which represents an investment of the capital stock of a corporation, or of any part thereof, cannot be regarded as surplus profits, and distributed as dividends, irrespective of the financial condition of the corporation. When a person subscribes for or purchases shares of stock in a corporation, and pays a part only of the amount due thereon, and the shares are afterwards forfeited for nonpayment of the balance, the amount paid is not profits, but a part of the capital, and cannot be divided among the stockholders.<sup>33</sup>

Mills, 6 Biss. 98, Fed. Cas. No. 8,974; St. John v. Erie Ry. Co., 10 Blatchf. 271, Fed. Cas. No. 12,226, 22 Wall. 136, 2 Keener's Cas. 1348; Barry v. Merchants' Exchange Co., 1 Sandf. Ch. (N. Y.) 280; Miller v. Bradish, 69 Iowa, 278; Hubbard v. Weare, 79 Iowa, 678; Mobile & Ohio R. Co. v. Tennessee, 153 U. S. 486, 2 Keener's Cas. 1295; Williams v. Western Union Telegraph Co., 93 N. Y. 162, 2 Keener's Cas. 1310, 2 Cum. Cas. 209; Phillips v. Eastern R. Co., 138 Mass. 122; In re London & General Bank, 72 Law T. (N. S.) 227; Belfast & Moosehead Lake R. Co. v. City of Belfast, 77 Me. 445; Ryan v. Leavenworth, Atchison & N. W. Ry. Co., 21 Kan.

365; Russell v. Bristol, 49 Conn.

"The assets, resources and funds of the corporation must consist of cash on hand and other property, and, if such assets exceed the liabilities, a dividend can be lawfully declared;" in other words, a profit exists." Hubbard v. Weare, 79 Iowa. 678.

<sup>31</sup> Per Sanford, Vice Chancellor, in Barry v. Merchants' Exchange Co., 1 Sandf. Ch. (N. Y.) 280, 307.

<sup>32</sup> Mills v. Northern Ry. of Buenos Ayres Co., 5 Ch. App. 621, 1 Smith's Cas. 352. See infra, this section.

33 Gratz v. Redd, 4 B. Mon. (Ky.) 178.

As has been shown in other sections, the stockholders of a corporation have the right to a division of its capital among them, after payment of its debts, when the corporation has been dissolved.34 And when the amount of the capital stock of a corporation has been reduced under legislative authority, they are entitled to a distribution of the excess of the actual capital over the amount of the stock as reduced.35 The fund thus distributed is sometimes called a "dividend," but it is very different from a dividend out of profits.

(c) Deduction of expenses and liabilities.—In addition to deducting the amount of the capital stock from the value of the assets of the corporation, deduction must also, as a rule, be made for all expenses and debts of the corporation. "The term 'profits,' out of which dividends alone can properly be declared, denotes what remains after defraying every expense, including loans falling due, as well as the interest on such loans."36

When a corporation, like a railroad company, has a bonded debt, representing money which it has put into its plant or works, etc., it must pay the interest thereon out of its earnings

34 Ante, § 328(b). 35 Ante, § 411.

36 Mobile & Ohio R. Co. v. Tennessee, 153 U. S. 486, 2 Keener's Cas. 1295. See, also, Hubbard v. Weare, 79 Iowa, 678; Corry v. Longery of the control of the donderry & Enniskillen Ry. Co., 29

In Hubbard v. Weare, 79 Iowa, 678, it was held that, where the statement of profits for the purpose of declaring dividends in-cludes as an asset "accrued interest on bills receivable," an approximation should be made of the accrued interest on bills payable, for which the company would be lia-

Speaking of a railroad company, it was said by Judge Blatchford: "Net earnings are, properly, the gross receipts, less the expenses of operating the road to earn such reout of what thus remains that is, right to declare a dividend. out of the net earnings. Many oth- sell v. Bristol, 49 Conn. 251.

er liabilities are paid out of the net earnings. When all liabilities are paid, either out of the gross receipts or out of the net earnings, the remainder is the profit of the shareholders, to go towards dividends, which, in that way, are paid out of the net earnings." St. John v. Erie Ry. Co., 10 Blatchf. 271, Fed. Cas. No. 12,226, affirmed in 22 Wall. (U.S.) 136, 2 Keener's Cas. 1348.

Where an insurance company is authorized to establish a guaranty fund in approved notes, to be used only for paying claims, and any part so used is to be refunded out of the first surplus receipts, and raises such a fund by subscription of the shareholders, under agreement that it is not to be resorted to until all the company's resources are exhausted, the fund cannot be reckoned with the comceipts. Interest on debts is paid pany's assets, to determine its before payment of a dividend;<sup>37</sup> but it need not pay the bonded indebtedness, for this is represented by its assets.<sup>38</sup> A sinking fund, however, should be provided for the payment of the bonded indebtedness as it falls due.<sup>39</sup>

- (d) Time of determining profits.—Whether or not there were surplus profits, so as to render it lawful to declare a dividend, is to be determined as of the time when the dividend was made. If the condition of the company at that time was apparently such as to show surplus profits out of which a dividend could lawfully be paid, the payment of the dividend is not rendered wrongful by the fact that debtors of the company who were then considered solvent afterwards became insolvent, and the company sustained losses, 40 or because, for any other reason, the conditions existing at the time the dividend was paid were such, unknown to the directors, that losses were sure to be sustained. 41
- (e) Money due but not received.—It has been held that the profits of a corporation, out of which dividends may be paid, do not include earnings which have not yet been received by the corporation, even though they may consist in money which is due, and which will undoubtedly be paid. Thus, in California, where a statute prohibits the payment of dividends except out of surplus profits, it was held that it was not proper, in determining the profits, to consider interest which had accrued upon bonds secured by a mortgage, but which was not payable, or interest thereon which was payable, but which had not been paid. 42
  - (f) Borrowed money.—If a corporation borrows money, the
- 87 Mobile & Ohio R. Co. v. Tennessee, 153 U. S. 486, 2 Keener's Cas. 1295. And see Gratz v. Redd, 4 B. Mon. (Ky.) 188.
- 38 Mills v. Northern Ry. of Buenos Ayres Co., 5 Ch. App. 621, 1 Smith's Cas. 352.
- <sup>39</sup> See Gratz v. Redd, 4 B. Mon. (Ky.) 188; Hazeltine v. Belfast & Moosehead Lake R. Co., 79 Me. 411, 1 Am. St. Rep. 330.
- 40 Main v. Mills, 6 Biss. 98, Fed. Cas. No. 8,974. And see Le Roy v. Globe Ins. Co., 2 Edw. Ch. (N. Y.)

- 657, 1 Smith's Cas. 325, 2 Keener's Cas. 1327; Reid v. Eatonton Mfg. Co., 40 Ga. 98, 2 Am. Rep. 563.

  41 Stringer's Case (In re Mercan-
- 41 Stringer's Case (In re Mercantile Trading Co.), 4 Ch. App. 475, 1 Smith's Cas. 334, 2 Keener's Cas. 1281.
- 42 People v. San Francisco Savings Union, 72 Cal. 199. "Money earned as interest," said the court in this case, "however well secured, or certain to be eventually paid cannot in fact be distributed as dividends to stockholders, and does not constitute surplus profits."

indebtedness therefor offsets the fund borrowed, and as a general rule, therefore, money cannot be borrowed for the purpose of paying dividends.43

It has been held, however, that when a corporation has used profits out of which it might have paid a dividend in the improvement of its property, when it might have borrowed the money for such purposes, it may borrow the money to take the place of the profits so used, and use it in paying the dividend, for the dividend in such a case is paid, in effect, out of the profits.44 And if surplus profits have in fact been earned, and are invested in property used in the business of the corporation, or other assets not at present available for the purpose of distribution among the stockholders as a dividend, a dividend may properly be paid by borrowing money.45 "A company," said Judge Kekewich, "is quite as competent to declare dividends out of property which is invested for the time being in buildings, or anything else, as it is out of cash in hand, and it is not necessary that a company, any more than an individual, should have cash at the bank on which it can draw in order to declare dividends."46

(g) Creation of reserve fund for repairs, etc.—In the case of railroad companies and other corporations whose capital stock is invested in rolling stock, tracks, buildings, machinery, or other property which must become worn and depreciated in value in its use, and which will have to be repaired or renewed from time to time, the wear of the property and necessity for repairs must be taken into consideration in estimating profits for the purpose of declaring dividends, and a sufficient sum must be set aside to create a reserve fund for repairs and renewals.47

ing Co., 2 Utah, 74.

<sup>44</sup> Excelsior Water & Mining Co. v. Pierce, 90 Cal. 131.

<sup>45</sup> Stringer's Case (In re Mercan-\* tile Trading Co.), 4 Ch. App. 475, 1 Smith's Cas. 334, 2 Keener's Cas. 1281; Corry v. Londonderry & Enniskillen Ry. Co., 29 Beav. 263; Mills v. Northern Ry. of Buenos

<sup>48</sup> Davis v. Flagstaff Silver Min- Ayres Co., 5 Ch. App. 621, 1 Smith's Cas. 352.

<sup>46</sup> Municipal Freehold Land Co. v. Pollington, 63 Law T. (N. S.)

<sup>47</sup> Davidson v. Gillies, 16 Ch. Div. 347, note, 2 Keener's Cas. 1362, 2 Cum. Cas. 223. See, also, Whittaker v. Amwell Nat. Bank, 52 N. J. 400.

But where a corporation allows

- (h) Insurance companies.—In estimating the surplus profits of an insurance company for the purpose of determining the amount which may lawfully be paid in dividends, it is not proper to regard as profits premiums paid, but not yet earned, without taking into consideration probable losses upon existing policies, for the unearned premiums and the interest upon the capital stock, and not the capital stock, is the primary fund out of which losses on existing risks are to be paid. In a Kentucky case the court went so far as to hold that unearned premiums could not be counted at all as surplus profits.48 The better rule, however, is that laid down in several New York cases.that unearned premiums may be included in the computation of profits, for the purpose of declaring a dividend, provided a sufficient surplus is retained, over and above the capital stock, to pay all probable losses on existing risks.49
- (i) Corporations whose property is necessarily consumed in use -Mining companies.-When a corporation is created for the purpose of investing its capital in property which will necessarily be consumed or exhausted in the course of its operations, so that the depreciation in the value of the property cannot be repaired, as in the case of a mining company, it is not subject to the same rules as other corporations. A mining company is not formed for the purpose of permanently using the property in which its capital is invested, but for the purpose of investing in property which, in the nature of things, will be gradually consumed in making profits, and, in estimating the profits of such a corporation for the purpose of determining whether it may lawfully declare a dividend, no deduction is to be made for depreciation in the value of its mine by reason of its use

its property to get out of repair, of the particular year only. See and pays dividends to ordinary post, § 529(c). shareholders without setting apart sary repairs and renewals, it can this section, (i). not, in a subsequent year, set apart

48 Lexington Life, Fire & Marine such a fund, not only for the curIns. Co. v. Page, 17 B. Mon (Ky.) rent year, but also for preceding 412, 66 Am. Dec. 165. years, and thus defeat the payment of a dividend to preferred Ins. Co., 6 Paige (N. Y.) 486;
shareholders, whose right to diviScott v. Eagle Fire Co., 7 Paige dends is dependent upon the profits (N. Y.) 198.

As to the different rule applicaany reserve fund for making neces- ble to mining companies, see infra,

and consumption in taking out the ore or other minerals. Dividends may be lawfully declared out of the net proceeds of its operations after deducting expenses and debts and a reasonable fund for contingencies.50

A mining company, however, cannot lawfully sell a part of its mine and declare a dividend out of the proceeds,51 or borrow money for the purpose of paying a dividend. 52

-- Other corporations within this rule.—The rule governing mining companies also applies to other corporations created for the purpose of using a property which must necessarily become exhausted in its use, as, for example, a corporation created for the purpose of utilizing a lease for a term of years, or a patent.<sup>53</sup>

(j) Valuation of property.—In placing a valuation upon property of a corporation in which its capital has been invested, the property may be considered as representing the amount invested, after deducting a fair allowance for depreciation in value by reason of wear and tear and other causes.<sup>54</sup>

In estimating the assets of a corporation, and the value thereof, for the purpose of determining the profits, care must be taken not to include the same item twice, as by including expenses paid and other items as separate assets, when they go to make up the estimated aggregate value of the corporate property. And it is also necessary, in fixing the value of particular assets, to make a proper allowance for probable loss. Iowa case it was held that, in stating the profits of a corporation for the purpose of declaring a dividend, money paid out for moving machinery or materials which went into the buildings of the corporation should be included in the assets, but not as a separate item, where the aggregate value of the buildings is given; that expenses of perfecting a machine should not be in-

<sup>50</sup> Excelsior Water & Mining Co. v. Pierce, 90 Cal. 131. See, also, Lee v. Neuchatel Asphalte Co., 41 Ch. Div. 1; Lambert v. Neuchatel Asphalte Co., 51 L. J. Ch. 882.

ing Co., 2 Utah, 74.

<sup>52</sup> Davis v. Flagstaff Silver Mining Co., 2 Utah, 74.

<sup>53</sup> See the dictum in Excelsior Water & Mining Co. v. Pierce, 90 Cal. 131.

<sup>54</sup> Mills v. Northern Ry. of Bue-51 Davis v. Flagstaff Silver Min- nos Ayres Co., 5 Ch. App. 621, 1 Smith's Cas. 352.

cluded as an asset until it is known that the machine will be successful, where its sole value depends upon that contingency; that money paid out for expenses should not be included as an asset, since, if the value of the corporate property is enhanced thereby, it is included in the statement of the value of the property; that profits of a former season should not be stated as a separate item in the statement of the assets of the corporation for a certain year, where such profits have not been declared or withdrawn from the general assets, as they are a part thereof; that outstanding accounts should not be stated as an asset, without approximating the amount to be deducted for loss; and that expenses for exhibiting a machine should not be included in the assets as a separate item, as they enter into the value of the general assets.55

The supreme court of the United States has held that the expression "profits of a business" means the receipts, deductng current expenses, and is equivalent to "net receipts;" and that depreciation of buildings in which the business is carried on, although they were erected by expenditure of the capital invested, is not ordinarily or necessarily considered in estimating the profits.56

#### Interest and interest dividends.

The rule that a corporation cannot reduce its capital stock by distributing any part of the same among its stockholders prevents a corporation from entering into an agreement to pay its stockholders interest upon the amount paid in by them on their shares, if there are no means except the capital stock out of which the interest can be paid, for the effect of such a transaction is to distribute among the stockholders a part of the capital stock.57

678.

56 Eyster v. Centennial Board of Finance, 94 U.S. 500.

Mich. 76, 18 Am. Rep. 156, 2 Keen-

55 Hubbard v. Weare, 79 Iowa, er's Cas. 1354; Painesville & Hudson R. Co. v. King, 17 Ohio St. 534; Pittsburg & Connellsville R. Co. v. 56 Eyster v. Centennial Board of inance, 94 U. S. 500.

57 Lockhart v. Van Alstyne, 31

Allegheny County, 63 Pa. St. 126; Troy & Boston R. Co. v. Tibbits, 18 Barb. (N. Y.) 297.

As to the right to interest on

There is nothing, however, to prevent a corporation from agreeing to pay its shareholders interest out of surplus or net profits, out of which it would be lawful for it to pay dividends, for this "is not more withdrawing capital from the corporation than would be the payment of ordinary dividends, to which purpose the fund would otherwise be appropriated."58 And an agreement by a corporation to pay its stockholders interest on the amount paid in on their shares, if it fixes no time for payment, is to be construed as an agreement to pay out of profits when earned 59

It has been held that, where stockholders of a corporation pay in part of their subscription before it is due or calls are made. the corporation may lawfully pay interest thereon, for this is in effect a loan by the stockholders, and not a contribution to the capital stock.60

### Set-off of dividends against debts due from stockholders. -A corporation has the right to apply dividends in its hands upon debts due to it from the stockholders entitled thereto.

Since a corporation is merely a debtor to its stockholders after a dividend is declared, it is well settled that it has the right of set-off as against stockholders who are indebted to it, and therefore, when a corporation is indebted to a stockholder for a dividend, and a debt is due to it from the stockholder, it may apply the dividend in satisfaction of the debt. 61

It is necessary, of course, in order that the right of set-off may exist, that a debt shall be actually due from the stockholder

clared, see post, § 527(c) (8).

58 Richardson v. Vermont & Massachusetts R. Co., 44 Vt. 613; McLaughlin v. Detroit & Milwaukee Ry. Co., 8 Mich. 100; Rutland & Burlington R. Co. v. Thrall, 35 Vt.

643. Evansvilla Indianapolis & C. 543; Evansville, Indianapolis & C. S. L. R. Co. v. City of Evansville, 15 Ind. 414; Wright v. Vermont & Massachusetts R. Co., 12 Cush. App. Cas. 461. And see other cases (Mass.) 75; Waterman v. Troy & in the notes preceding. See, also, Greenfield R. Co., 8 Gray (Mass.) ante. § 467(d). 433; Cunningham v. Vermont &

dividends after they have been declared, see post, § 527(c)(8). (Mass.) 411; Barnard v. Vermont & Massachusetts R. Co., 7 Allen (Mass.) 512.

59 Rutland & Burlington R. Co. v. Thrall, 35 Vt. 543; Waterman v. Troy & Greenfield R. Co., 8 Gray (Mass.) 433.

60 Lock v. Queensland Investment & Land Mortgage Co. [1896] App. Cas. 461. And see other cases ante. § 467(d).
61 Gemmell v. Davis, 75 Md. 546,

And the debt must be due from the stockholder himself only, and not due jointly from him and another. A corporation cannot apply dividends due to an individual stockholder to the payment of a debt due to the corporation from a partnership of which he is a member.<sup>63</sup>

Effect of transfer of stock.—The right of set-off exists only where the indebted shareholder owns the stock at the time the dividend is declared. If he has transferred it before the declaration of the dividend, and the transfer has been duly registered, or notice thereof given to the corporation, the corporation must pay the dividend to the transferee, notwithstanding its claim against the transferrer, for a corporation has no lien on the shares of its stockholders.<sup>64</sup> The right of one to whom stock

32 Am. St. Rep. 412; Hagar v. Union Nat. Bank, 63 Me. 509; Sargent v. Franklin Ins. Co., 8 Pick. (Mass.) 90, 19 Am. Dec. 306; Philadelphia, Wilmington & B. R. Co. v. Cowell, 28 Pa. St. 329, 70 Am. Dec. 128; Bates v. New York Ins. Co., 3 Johns. Cas. (N. Y.) 238; King v. Paterson & Hudson River R. Co., 29 N. J. Law, 504, 2 Keener's Cas. 1330; Donnally v. Hearndon, 41 W. Va. 519; First Nat. Bank of Texarkana v. De Morse (Tex.) 26 S. W. 417. Compare Attorney General v. State Bank, 1 Dev. & B. Eq. (N. C.) 545; Ex parte Winsor, 3 Story, 411, Fed. Cas. No. 17,884.

62 A corporation cannot collect out of a dividend, without the consent of the stockholder, an unauthorized assessment. Ex parte Winsor, 3 Story, 411, Fed. Cas. No. 17,884.

Where a resolution of the directors of a bank provided that a dividend declared should be entered as a credit on the debt of any shareholder "whose indebtedness is not fully secured," it was held that the dividend of a director could not be appropriated to the payment of a note upon which he was surety, where, when the divi-

dend was declared, the note was secured by collateral, and several days afterwards the bank, with the consent of the surety, surrendered the collateral, and accepted from the principal, as security for the note and an additional debt of the principal, a trust deed of land reciting that the note was extended for twelve months. Solomon v. First Nat. Bank of Meridian, 72 Miss. 854.

A corporation has no right to set off dividends against a debt guarantied by a stockholder, but which is not yet due. First Nat. Bank of Texarkana v. De Morse (Tex.) 26 S. W. 417.

63 American Nat. Bank v. Nashville Warehouse & Elevator Co. (Tenn. Ch. App.) 36 S. W. 960.

<sup>64</sup> Gemmell v. Davis, 75 Md. 546, 32 Am. St. Rep. 412; American Nat. Bank v. Nashville Warehouse & Elevator Co. (Tenn. Ch. App.) 36 S. W. 960. And see Brent v. Bank of Washington, 2 Cranch, C. C. 517, Fed. Cas. No. 1,834. Compare Bellevue Bank v. Higbee, 4 Ohio Cir. Ct. R. 222.

payment of a note upon which he That a corporation has no lien was surety, where, when the divion shares, see post, § 573 et seq.

is pledged before declaration of a dividend is superior to any right of set-off by the corporation, if it has notice of the pledge.65

A by-law of the corporation providing that the stock shall be transferable only on the books of the company, being for the protection of the company only in the payment of dividends, etc.,66 does not entitle it to set off the dividends due a stockholder in payment of a debt due from him, if it had actual notice of a transfer of the stock by him before declaration of the dividend.67

§ 523. Mode of declaring and paying dividends—(a) In general.—Unless there is some charter or statutory provision to the contrary, dividends can be declared only by formal action of the board of directors, entered upon the records of the corporation.

Unless otherwise provided, it is within the discretion of the directors of a corporation to pay dividends either in cash, or property, or bonds, or, if there is stock in reserve, or the capital stock may be increased, in stock; but if a dividend be made payable in cash or payable generally, the debt must be paid in lawful currency.

No discrimination can be made between stockholders in the mode of paying dividends.

(b) Mode of declaring dividend—In general.—A dividend can only be declared by formal action of the board of directors, or of the stockholders as a body, as the case may be, and the vote must appear on the records of the corporation. 68 The declaration of a dividend cannot be proved by parol evidence in collateral suits between the corporation and stockholders, but only

In a New York case, where a stockholder in an insurance company, who had given notes to the company, transferred his stock, it Gedge, 96 Ky. 513; Dennis v. Joslin was held that the company had a Mfg. Co., 19 R. I. 666, 61 Am. St. right to apply dividends accruing Rep. 805, 2 Keener's Cas. 1346.

65 Gemmell v. Davis, 75 Md. 546, on the stock to the payment of one of the notes which fell due before it had any notice of the transfer, since until then the transfer was not good as against the company. but that it could not apply them to notes falling due after notice of the transfer. Bates v. New York Ins. Co., 3 Johns. Cas. (N. Y.) 238.

68 American Wire Nail Co. v.

<sup>32</sup> Am. St. Rep. 412.

<sup>66</sup> Post, § 585 et seq.

<sup>67</sup> American Nat. Bank v. Nashville Warehouse & Elevator Co. (Tenn. Ch. App.) 36 S. W. 960.

by the corporate records. If a dividend has in fact been declared, but does not appear on the records, the remedy is to correct the records, first in the corporation itself, by calling attention to the omission, or, where this will not avail, by mandamus to the proper officer, or by a suit in equity. "Where, as in the matter of a dividend," said the Rhode Island court, "members of a corporation have a common interest and right by virtue of action taken, the record should show what the corporation did, and in case of error the remedy should be a proceeding to correct the record itself, rather than by parol evidence in collateral suits, which would be liable to different results. It follows that the parol evidence offered in this case to show that a dividend was voted as an offset to advances, is inadmissible."69

In declaring dividends, the corporation must comply, both as to mode and time, with any express provisions in the charter or general law.\*

(c) Cash or property dividends.—"There is no rule of law or reason founded upon public policy which condemns a property dividend. The directors could convert the property into cash before a dividend and divide that. So the stockholders can take the property divided to them and sell it and thus realize the cash. Within the domain of law, it can make no material

69 Dennis v. Joslin Mfg. Co., 19 R. I. 666, 61 Am. St. Rep. 805, 2

Keener's Cas. 1346. \*Under the New Jersey corporation act (section 47), which proaccumulated profits of a corporation, less the amount reserved for working capital, in dividends in January of each year, "unless some specific day or days for that purprovides that dividends on its common stock shall be declared after the close of any fiscal year has no previous to the close of a fiscal quaryear. Marquand y. Federal Steel 725. Co., 95 Fed. 725.

Such provision applies to dividends on preferred stock, as well as to dividends on common stock. While the statute (Laws 1896, p. 283, § 18) permits the payment of vides for the distribution of all dividends on preferred stock quarterly or semiannually, it does not affect the requirement that the specific day or days for declaring such dividends must be fixed by the charter or by-laws. If they are pose be fixed in its charter or by- not so fixed, the directors have no laws," a corporation whose charter power to declare dividends on preferred stock on days selected in their discretion; nor can the articles of incorporation give them power to declare such dividends such discretionary power. Marquand v. Federal Steel Co., 95 Fed. difference which course is pursued. If, however, a dividend be made payable in cash or payable generally, the corporation becomes a debtor, and must discharge such debt, as it is bound to discharge all its other debts, in lawful currency. It is true that a stockholder cannot be compelled to receive property divided to him. So he cannot be compelled to take a cash dividend. In case of his refusal to take a cash dividend, the corporation may retain it for him until he shall demand it. case he shall refuse to take a property dividend, the corporation may retain it and hold it in trust for him, or possibly sell it for his benefit."70

Cash payment of dividends may be required by the charter of the corporation or by some other statute, by the articles of association, or by the contracts of subscription to its stock.<sup>71</sup>

The directors of a corporation may make dividends payable at a banking house in good credit, giving proper notice to the stockholders of the deposit there made to their credit, and if a stockholder, after receipt of the notice, neglects to draw the money within a reasonable time, and the bank fails, the loss falls upon him, and not upon the corporation.72

(d) Bond or scrip dividends.—In the absence of statutory provision to the contrary, a corporation may use surplus profits in improvement of its property or in purchasing machinery or other property which it is authorized under its charter to acquire and hold, and issue its bonds in payment of the dividend from such profits. 73 Or it may issue a scrip dividend. Scrip is

70 Williams v. Western Union River R. Co., 29 N. J. Law, 82, 504, Telegraph Co., 93 N. Y. 162, 2 Keener's Cas. 1310, 2 Cum. Cas.

Keener's Cas. 1310, 2 Cum. Cas. Where the directors of a corpo209. See Ehle v. Chittenango Bank, ration deposit a dividend in a bank 24 N. Y. 548; Scott v. Central Railroad & Banking Co. of Georgia, 52 Barb. (N. Y.) 45.

Distribution of land. See Merchant v. Western Land Ass'n, 56 Minn. 327; Olsen v. Homestead Land & Improvement Co., 87 Tex.

71 See State v. Baltimore & Ohio R. Co., 6 Gill (Md.) 363.

72 King v. Paterson & Hudson Co., 6 Gill (Md.) 363.

in good credit to the account of the stockholders, and the bank fails after the stockholder has had a reasonable time to draw his money, the company must show that due notice of the deposit was given to the stockholder. King v. Paterson & Hudson River R. Co., 29 N. J. Law, 82, 504, 2 Keener's Cas.

73 State v. Baltimore & Ohio R.

simply a writing or certificate issued to shareholders in lieu of a dividend, entitling them to money, stock, bonds, land, or other benefit at some future time,—"an interim or provisional document or certificate, to be exchanged, when certain payments have been made or conditions complied with, for a more formal certificate, as of shares or bonds, or entitling the holder to the payment of interest, a dividend, or the like."<sup>74</sup>

The issuing of a bond or scrip dividend by a corporation to represent an investment of bona fide profits is not prohibited by a statute requiring dividends to be made only from surplus profits of the corporation, and providing that it shall not be lawful for corporations to divide or pay to stockholders any part of the capital, or to reduce the capital stock. Nor is such a dividend contrary to public policy.<sup>75</sup>

(e) Stock dividends.—A stock dividend is a dividend payable in reserved or additional stock of the corporation, instead of in cash or in property.\* If a corporation has issued all the shares of stock which its charter authorizes it to issue, and has no authority to increase its capital stock, it is clear that it cannot increase its capital stock by retaining surplus profits in its business, and paying a dividend by issuing additional stock therefor. It is otherwise, however, when a corporation has in reserve stock which it can lawfully issue, or when it is authorized to increase its capital stock. In such a case, in the absence of a constitutional or statutory prohibition, if the directors of the corporation, acting in good faith, are of the opinion that it is for the best interests of the corporation and its stockholders to retain profits in the business of the corporation, or as a surplus fund to meet future needs, instead of dividing them among the

<sup>74</sup> Century Dict. & Cyc. "Scrip." See Rogers v. New York & Texas Land Co., 134 N. Y. 197; State v. Baltimore & Ohio R. Co., 6 Gill (Md.) 363; Williams v. Western Union Telegraph Co., 61 How. Pr. (N. Y.) 216, 9 Abb. N. C. 437, 93 N. Y. 162, 2 Keener's Cas. 1310, 2 Cum. Cas. 209; Chaffee v. Rutland R. Co., 55 Vt. 110.

<sup>75</sup> Williams v. Western Union Telegraph Co., 61 How. Pr. (N. Y.) 216, 9 Abb. N. C. 437, 93 N. Y. 162, 2 Keener's Cas. 1310, 2 Cum. Cas. 209.

<sup>\*</sup>As to what constitutes a dividend for the purposes of taxation, see ante, § 286(d), and the cases there collected.

stockholders as a dividend in cash or property, it is within their discretion to do so, and to pay a dividend by issuing reserved or additional stock. Such a dividend is not in any sense a distribution of the capital stock of the corporation among the stockholders, so long as the amount of stock issued does not exceed the amount of the profits out of which it is lawful to declare a dividend.76 In some jurisdictions there are constitutional or statutory prohibitions against issuing stock dividends, or limitations upon the power to issue them.<sup>77</sup>

While it is necessary to a valid stock dividend that the conditions shall be such as to make it to the interest of the corporation to retain the surplus profits in the business of the corporation, instead of distributing them among the shareholders, whether the best interests of the corporation require this is to be determined primarily by the directors, and the courts will not interfere with or control the exercise of their discretion in this respect, so long as they act in good faith and reasonably; but if they act in bad faith or arbitrarily, and declare a stock dividend when the interests of the corporation do not require them to retain the surplus profits in its business, a court of equity will interfere to protect the rights of stockholders.<sup>78</sup>

76 Williams v. Western Union 78 Va. 501, 2 Keener's Cas. 1384; Telegraph Co., 93 N. Y. 162, 2 Keen-Parker v. Mason, 8 R. I. 427. er's Cas. 1310, 2 Cum. Cas. 209; Jones v. Terre Haute & Richmond R. Co., 57 N. Y. 196; Howell v. Chicago & North Western Ry. Co., 51 Barb. (N. Y.) 378; Gibbons v. Mahon, 136 U. S. 549; Rand v. Hubbell, 115 Mass. 471; Davis v. Jackson, 152 Mass. 58, 23 Am. St. Rep. 801; Terry v. Eagle Lock Co., 47 Conn. 141; Farwell v. Great Western Telegraph Co., 161 Ill. 522; Kenton Furnace, Railroad & Manufacturing Co. v. McAlpin, 5 Fed. 743; Brown v. Lehigh Coal & Navigation Co., 49 Pa. St. 270; Com. v. Pittsburg, Fort Wayne & C. Ry. Co., 74 Pa. St. 83; Dock v. Schlichter Jute Cordage Co., 167 Pa. St. 370; Waterman v. Alden, 42 Ill. App. 294; Gordon's Ex'rs v. Richmond, Fredericksburg & P. R. Co., er's Cas. 1310, 2 Cum. Cas. 209;

Parker v. Mason, 8 R. I. 427.

A dividend representing profits may be made payable either in cash or in increased stock, at the option of stockholders. Such a dividend is not a mere substitute for a stock dividend, when the stockholder is at liberty to sell his right to subscribe for the new stock. Davis v. Jackson, 152 Mass. 58, 23 Am. St. Rep. 801.

77 Distribution by a corporation, under statutory authority, of shares of stock purchased by it from the state, is not a violation of a statute forbidding declaration of a stock dividend without authority from a court. Com. v. Boston & Albany R. Co., 142 Mass. 146.

78 Williams v. Western Union Telegraph Co., 93 N. Y. 162, 2 Keen-

If the charter of a corporation requires it to pay dividends in cash, it cannot declare a stock dividend and compel its shareholders to accept the new stock instead of cash; and its obligation to pay in cash is not affected by statutory authority to increase its capital stock, or to liquidate its indebtedness by issuing preferred stock.79

There must be surplus profits.—As in the case of a cash or property dividend, a stock dividend can only be assued to represent surplus profits. The assets of the corporation, over and above its debts, etc., must be equal to the amount of the new stock added to the amount of the original capital stock.80

Under a constitutional or statutory provision that no corporation shall issue stock except for money, labor done, or money or property actually received, and all fictitious increase of stock shall be void, it was held that a corporation with a capital stock of ten thousand dollars had no authority to double its capital stock, and distribute the new stock among its stockholders as a stock dividend, on the mere statement that its capital stock "has been invested in property which has more than doubled in value, and is now worth \$20,000 over and above all liabilities."81

Revocation of declaration.—It has been held that a vote of

and other cases cited above. See, dend in stock instead of cash, also, ante, § 517(f).

79 Hardin County v. Louisville & Nashville R. Co., 92 Ky. 412. In this case it was held that a statute amending the charter of a railroad company, and providing that it should allow all stockholders interest on their stock from the time of paying for the same to the time of making the first dividend, made it obligatory upon the company to pay such dividend in cash, and that this obligation was not affected by a statute authorizing it to increase its capital stock to an amount sufficient to represent the full cost of its road, and to liquidate its indebtedness by issuing preferred stock.

against the dissent of a stockholder, where such a mode of payment is contrary to the provisions of its charter, or of a statute, or where the stockholders are entitled to cash dividends, and the shares which it is proposed to issue are of less value than the amount to which they are entitled. Hoole v. Great Western Ry. Co., 3 Ch. App. 262, 2 Keener's Cas. 1302.

80 Williams v. Western Union Telegraph Co., 93 N. Y. 162, 2 Keener's Cas. 1310, 2 Cum. Cas. 209. And see Howell v. Chicago & North Western Ry. Co., 51 Barb. (N. Y.) 378.

81 Fitzpatrick v. Dispatch Publishing Co., 83 Ala. 604. And see A corporation cannot pay a divi- Parsons v. Joseph, 92 Ala. 403.

a corporation declaring a stock dividend does not give a stockholder a vested interest in the stock, as in the case of the declaration of a cash dividend by the directors, so as to prevent a subsequent vote rescinding the declaration.82

-Recovery of dividend in money.-If a corporation has declared a stock dividend, a stockholder cannot make it the basis of an action against the corporation to recover his dividend in money, for in bringing the action he ratifies the dividend, and can only recover it as declared.83

Persons entitled to dividend.—As we shall see in a subsequent section, stock dividends, like cash dividends, belong, in the absence of agreement to the contrary, to the holders of stock at the time the dividend is declared, without regard to the time when the dividend is payable, and without regard to the source from which, or the time during which, the funds so divided among the stockholders were acquired.84 The right to a stock dividend as between a person entitled to the income only of shares and the remainderman will also be considered in a subsequent section.85

(f) Discrimination between stockholders.—A corporation has no right to discriminate between stockholders by paying some in gold, to the exclusion of others, or by paying some in cash, and others in property or stock, but must treat all alike.86 Where the board of directors of a corporation declared a dividend of a

Harris v. San Francisco Sugar Refining Co., 41 Cal. 393. Especially is this true where the stockholder has also ratified the dividend by recovering his share of the new stock. Harris v. San Francisco Sugar Refining Co., 41 Cal. 393.

84 Jermain v. Lake Shore & Michigan Southern Ry. Co., 91 N. Y. 483, 2 Keener's Cas. 1411. See post,

Holders of preferred stock are

s2 Terry v. Eagle Lock Co., 47 entitled to share in a stock dividend unless excluded by the terms of their contract. Gordon's Ex'rs Jute Cordage Co., 167 Pa. St. 370. v. Richmond, Fredericksburg & P. s3 State v. Baltimore & Ohio R. R. Co., 78 Va. 501, 2 Keener's Cas. Co., 6 Gill (Md.) 363. And see Harris v. San Evanciaco Susan Pa.

In Terry v. Eagle Lock Co., 47 Conn. 141, it was held that a suit by a stockholder to recover a stock dividend, brought a year after a vote rescinding the declaration of the dividend, was barred by the plaintiff's laches, where important transactions had intervened, and stock had changed hands on the basis of the unincreased capital. 85 Post, § 526(c)(6).

86 State v. Baltimore & Ohio R.

certain per cent., and gave to all stockholders holding less than fifty shares a right to a cash payment, but declared that stockholders holding more than fifty shares must accept part cash and part in bonds of the company, it was held that a stockholder of the latter class was not obliged to receive the bonds, but might treat the dividend, so far as the bonds were concerned, as illegal.87

In making a stock dividend, the corporation cannot, any more than in making a cash or property dividend, discriminate between its shareholders. Each shareholder is entitled to receive new shares in proportion to the stock held by him, and any discrimination is illegal.88

"The dividends must be general on all the stock, so that each stockholder will receive his proportionate share. The directors have no authority to declare a dividend on any other principle. They cannot exclude any portion of the stockholders from an equal participation in the profits of the company."89

### Time of payment of dividends.

It is within the discretion of the directors to fix the time for payment of a dividend. 90 If no time is fixed by the resolution declaring a dividend, it is payable on demand, 91 and if the resolution declares that it shall be payable at such time as the board of directors may direct, and the board fixes no time, the law implies that it shall be paid within a reasonable time. 92

# Persons who are entitled to dividends—(a) In general. -Every owner of shares of stock in a corporation at the time a

Co., 6 Gill (Md.) 363; Luling v. Atlantic Mutual Ins. Co., 45 Barb. (N. Y.) 510, 30 How. Pr. 69.

87 State v. Baltimore & Ohio R.

Co., 6 Gill (Md.) 363.

88 See Gray v. Portland Bank, 3 Mass. 364, 3 Am. Dec. 156; Jones v. Morrison, 31 Minn. 140; State v. Smith, 48 Vt. 289.

89 Ryder v. Alton & Sangamon R. Co., 13 Ill. 516.

90 Williams v. Western Union

Telegraph Co., 93 N. Y. 162, 2 Keener's Cas. 1310, 2 Cum. Cas.

91 State v. Baltimore & Ohio R. Co., 6 Gill (Md.) 363; Armant v. New Orleans & Carrollton R. Co., 41 La. Ann. 1020; Philadelphia, Wilmington & B. R. Co. v. Cowell, 28 Pa. St. 329, 70 Am. Dec. 128.

92 Beers v. Bridgeport Spring Co., 42 Conn. 17, 2 Keener's Cas.

1429.

dividend is declared is entitled to share ratably therein, unless there is some agreement to the contrary.

When shares are transferred, either absolutely or as collateral security, the transferee or pledgee is entitled, in the absence of agreement to the contrary, to all dividends declared after the transfer, but not to dividends declared before, although not payable until afterwards.

But if stock is transferrable only on the books of the company, the corporation will not be liable if it pays a dividend to the person appearing on the books as the owner of shares, although the shares may have been transferred, unless it has notice of the transfer.

A legatee of shares, unless the will provides otherwise, is entitled to dividends declared after the testator's death, but not to dividends declared before, although payable afterwards.

Where a will gives one the income of the estate, consisting in part of shares of stock, he is entitled to dividends declared after, but not to those declared before, the testator's death.

(b) All stockholders entitled to share pro rata.—It is an undoubted general rule that, in the absence of agreement to the contrary, all persons who own shares of stock in a corporation at the time a dividend is declared are entitled, as a matter of abso-. lute right, to share ratably in the dividend in proportion to their respective shares, regardless of the time when their shares were acquired, and the corporation cannot make any discrimination, or otherwise deprive any one of them of this right.93 One who

93 Jackson's Adm'r v. Newark der v. Alton & Sangamon R. Co., Plankroad Co., 31 N. J. Law, 277, 2 13 Ill. 516; Central Railroad & Keener's Cas. 1418, 2 Cum. Cas. Banking Co. v. Papot, 59 Ga. 342; 201; Jones v. Terre Haute & Richmond R. Co., 57 N. Y. 196, 29 Barb. (N. Y.) 353; Luling v. Atlantic Mutual Ins. Co., 45 Barb. (N. Y.) Where the by-laws of a steam-boat company required each stock-510; Boardman v. Lake Shore & holder to put a boat into its service and provided that if any boat Michigan Southern Ry. Co., 84 N. Y. 157, 2 Keener's Cas. 1368; Hill dry Co., 34 Conn. 542; March v. a stockholder who failed to repair Eastern R. Co., 43 N. H. 515; Ry- forfeited only so much of the divi-

ice, and provided that, if any boat should become unfit for service, the v. Newichawanick Co., 8 Hun (N. 459, affirmed 71 N. Y. 593; should cease until it should be re-Goodwin v. Hardy, 57 Me. 143; paired, or another should be furstate v. Baltimore & Ohio R. Co., nished, but that the proportion of 6 Gill (Md.) 363; Phelps v. Farm-ers' & Mechanics' Bank, 26 Conn-269; Stoddard v. Shetucket Foun-paid to the owner, it was held that receives stock from a corporation immediately before a dividend is declared has the same right as the other stockholders to share therein, unless he is excluded by the terms of his contract.94

"A person holding, as owner, the stock of a corporation, becomes thereby entitled to a proportionate share in the profits of the company, and consequently, a duty is imposed by law on the body corporate to distribute all dividends which, from time to time, may be declared, ratably on all its capital stock."95 "The dividends must be general on all stock, so that each stockholder will receive his proportionate share. The directors have no authority to declare a dividend on any other principle. They cannot exclude any portion of the stockholders from an equal participation in-the profits of the company."96

The fact that a corporation has never issued a certificate of stock to a shareholder does not affect his right to dividends.97

---Stock dividends.-The rule that all persons who own stock at the time a dividend is declared are entitled to share therein in proportion to their stock, and that it is unlawful for a corporation to make any discrimination, applies to stock dividends, as well as to dividends payable in cash, property, bonds, or scrip.98

# (c) Rights on transfer of stock—(1) In general.—As was ex-

dends as were earned during the default, whether they were declared during or after the default. Bigbee & Warrior River Packet Co. v. Moore, 121 Ala. 379.

It was also held that a provision in the by-laws allowing the company, after notice, to repair at the owner's expense, on his failure to repair, and appropriate his share of dividends for such purpose, did not impose on the company a duty to repair, but it could do so or not, at its option. Bibee v. Warrior River Packet Co. v. Moore, 121 Ala.

Of course, the holders of preferred or guarantied stock are entitled to preference over the holders of common stock. See post, § 529.

94 Jones v. Terre Haute & Richmond R. Co., 29 Barb. (N. Y.) 353, 57 N. Y. 196, where the holder of bonds of a corporation convertible at any time into stock exchanged them for stock just before the declaration of a dividend.

95 Jackson's Adm'r v. Newark Plankroad Co., 31 N. J. Law, 277, 2 Keener's Cas. 1418, 2 Cum. Cas.

96 Ryder v. Alton & Sangamon R.

Co., 13 III. 516.
97 Ellis v. Essex Merrimack
Bridge, 2 Pick. (Mass.) 243; Com. v. Springfield, M. & H. Turnpike Co., 10 Bush (Ky.) 257. See ante, § 378(b).

98 Gray v. Portland Bank, 3 Mass. 364, 3 Am. Dec. 156; Jones v. Morrison, 31 Minn. 140; State v. Smith,

48 Vt. 289.

plained in a previous section, the profits made by a corporation in the conduct of its business belong to the corporate body, and until a dividend has been declared, the individual stockholders have no legal right to any share therein, but after a dividend has been declared, each shareholder has a legal right to share in the dividend in proportion to his stock, and the relation between him and the corporation, to this extent, is that of debtor and It follows from this that, when shares of stock are transferred, and there is no agreement to the contrary, the transferee will be entitled, as an incident to his ownership of the stock, and without any separate assignment, to all dividends declared after the transfer, though the profits out of which they are declared may have been earned by the corporation before the transfer, while the transferrer is entitled to all dividends declared before the transfer, although they may not be payable until afterwards.99

"Stockholders," said Judge Jenkins in a federal case, "are,

99 Wheeler v. Sleigh Co., 39 Fed. 347, 2 Cum. Cas. 203; Bright v. Lord, 51 Ind. 272, 19 Am. Rep. 732, 1 Smith's Cas. 344, 2 Keener's Cas. 1408; Brundage v. Brundage, 60 N. Y. 544; Hill v. Newichawanick Co., 8 Hun (N. Y.) 459, 71 N. Y. 593; Kane v. Bloodgood, 7 Johns. Ch. (N. Y.) 90; Jones v. Terre Haute & Richmond R. Co., 57 N. Y. 196; Boardman v. Lake Shore & Michigan Southern Ry. Co., 84 N. Y. 157, 178, 2 Keen-er's Cas. 1368; Jermain v. Lake Shore & Michigan Southern Ry. Co., 91 N. Y. 483, 2 Keener's Cas. 1411; In re Kernochan, 104 N. Y. 618; Hopper v. Sage, 112 N. Y. 530, 8 Am. St. Rep. 771; Burroughs v. North Carolina R. Co., 67 N. C. 376, 12 Am. Rep. 611; Kaufman v. Charlottesville Woolen Mills, 93 Va. 673; Phelps v. Farmers' & Mechanics' Bank, 26 Conn. 269; Bates v. Md. 546, 32 Am. St. Rep. 412; Ryan paid before the transfer. Jermain v. Leavenworth, Atchison & N. W. v. Lake Shore & Michigan South-Ry. Co., 21 Kan. 365; March v. ern Ry. Co., 91 N. Y. 483, 2 Keen-Eastern R. Co., 43 N. H. 515; Foote er's Cas. 1411. See post, § 529(g).

Northwestern v. Worthington, 22 Pick (Mass.) 299; Cook v. Monroe, 45 Neb. 349; Central Railroad & Banking Co. v. Papot, 59 Ga. 342; Goodwin v. Hardy, 57 Me. 143, 99 Am. Dec. 758; King v. Follett, 3 Vt. 385; Waterman v. Alden, 42 Ill. App. 294; Richardson v. Richardson, 75 Me. 570, 46 Am. Rep. 428; Abercrombie v. Riddle, 3 Md. Ch. 320. See, also, Coleman v. Columbia Oil Co., 51 Pa. St. 74; Mann v. Ander-son, 106 Ga. 818; Price v. Morning Star Mining Co., 83 Mo. App. 470; Clark v. Campbell (Utah) 65 Pac.

> The rule is the same in England. Black v. Homersham, 4 Exch. Div.

This rule applies to preferred stock. If a dividend on preferred stock is not declared until after the stock is transferred, it belongs Androscoggin & Kennebec R. Co., to the transferee, although it 49 Me. 491; Gemmell v. Davis, 75 should have been declared and as to the property of the corporation, quasi partners, holding per my et per tout. The earnings of the corporation are part of the corporate property, held by the same tenure, and, until separated from the general mass, the interest of the stockholder therein passes with a transfer of the stock; and this, irrespective of the time during which earnings have accrued. By the declaration of a dividend, however, the earnings, to the extent declared, are separated from the general mass of property, and appropriated to the then stockholders, who become creditors of the corporation for the amount of the dividend. The relationship of the stockholder to the corporation, as to the amount of tne dividend, is thus changed from one of partnership ownership to that of creditor. He thereafter stands to the corporation in a dual relation,—with respect to his stock, as partner and part owner<sup>100</sup> of the corporate property; with respect to the dividend, as creditor upon a par with other creditors of the The severance of the earnings from the general corporation. mass of corporate property, and the promise to pay, arising from the declaration of the dividend, works this change. earnings represented by the dividend, although the fruit of the general property of the company, are no longer represented by the stock, but become a debt of the company to the individual who at the time of the declaration of dividend was the owner of the stock. That the dividend is payable at a future date can work no distinction in the right. The debt exists from the time of the declaration of dividend, although payment is postponed for the convenience of the company. The right became fixedabsolute by the declaration. This right could, of course, be transferred with the stock by special agreement, but not other-The dividend would not pass as an incident of the stock."101 In an English case, dividends which have been de-

100 The learned judge, of course, meant to refer to the stockholder's beneficial interest in the property of the corporation, for the le-

100 The learned judge, of course, gal title is not in him, but in the eant to refer to the stockhold-corporation. See ante, § 6.

101 Wheeler v. Northwestern Sleigh Co., 39 Fed. 347, 2 Cum. Cas. 203. clared are happily likened to fallen fruit, which does not pass under a sale or gift of the tree.102

This rule may be changed by the terms of the transfer or agreement of the parties. 103 A contract by the owner of stock to sell it on demand does not transfer the stock, and the other party, after a demand and completion of the sale, has no right to a dividend declared before the demand, though not payable until afterwards. 104

The rule may also be changed by statute, or by the corporation's charter or articles of association, or by the terms of the resolution declaring the dividend, as where the articles provide that a shareholder shall not receive any dividend after the period at which he ceases to be the owner of shares, but that dividends on such shares shall continue in suspense until some other person shall become the owner of them, 105 or, according to a North Carolina case, where the resolution declaring a dividend payable on a future date provides that the transfer books shall be closed for thirty days prior to such date. 106 By the

Ea. 283.

103 See Hancock v. Clark, 68 Vt. 302, where the vendor of stock reserved the right to dividends thereon until payment therefor.

Where stock is sold, to be delivered at the option of the seller, the purchaser, and not the seller, is entitled to a dividend declared after the sale and before delivery. Black v. Homersham, 4 Exch. Div. 24; Currie v. White, 45 N. Y. 822.

An agreement by which the seller of shares is to receive all dividends up to a certain time does not entitle him to a dividend, declared after that time, of profits earned during the time within which he was entitled to dividends, because a shareholder has no right to the profits of the corporation until a division is made or a dividend is declared. Hyatt v. Allen, 56 N. Y. 553, 15 Am. Rep. 449.

Where stock was assigned with a transfer of "all dividends made after the morning of the 23d of Sep- 611.

102 De Gendre v. Kent, L. R. 4 tember," both parties at the time expecting that a dividend would be made on the 22d of the month, but in fact it was not made until after the morning of the 23d, it was held that the dividend did not pass to the assignee. Brewster v. Lathrop, 15 Cal. 21.

Under a contract by which a party agreed to buy stock within a certain time if the owner should desire to sell, and which reserved to him all dividends declared during the time of the option, it was held that he was not entitled to a dividend declared before, though it was payable during, the time of the option. Hopper v. Sage, 112 N. Y. 530, 8 Am. St. Rep. 771, af-firming 47 N. Y. Super. Ct. 77. But see Harris v. Stevens, 7 N. H. 454.

104 Bright v. Lord, 51 Ind. 272, 19 Am. Rep. 732, 1 Smith's Cas. 344, 2 Keener's Cas. 1408.

105 Clive v. Clive, Kay, 600. 106 Burroughs v North Carolina R. Co., 67 N. C. 376, 12 Am. Rep.

weight of authority, however, in the absence of a charter or statutory provision to the contrary, the right of a transferee of shares to a dividend declared after the transfer is not affected by the fact that the transfer books are closed before the dividend is declared, if he gives the corporation notice of the transfer.<sup>107</sup>

Of course, a purchaser of stock in a corporation is not entitled to dividends declared after the purchase if he loses his right to the stock by failure to comply with the contract of purchase, for his right to the dividend depends upon his ownership of the stock.<sup>108</sup>

- —Stock dividends.—The rule that dividends belong, in the absence of an agreement to the contrary, to the holder of stock at the time the dividend is declared, without regard to the source from which, or the time during which, the funds were acquired, and without regard to the time when the dividend is payable, applies to stock dividends, as well as to cash dividends. 109
- —(2) Rights of pledgees.—In the absence of agreement to the contrary, a pledge of shares of stock as collateral security carries with it, as an incident of the pledgee's special ownership, the right to receive dividends afterwards declared, to be applied on the debt, or held in trust for the pledgor; and if the transfer has been registered on the books of the corporation, or, although not so registered, if the corporation has notice thereof, it will be liable to the pledgee if it pays such dividends to the pledgor. 111

107 Jones v. Terre Haute & Richmond R. Co., 57 N. Y. 196; Robinson v. New Berne Nat. Bank, 95 N. Y. 637, 2 Cum. Cas. 157. See infrathis section, (3).

108 Phinizy v. Murray, 83 Ga. 747,

20 Am. St. Rep. 342.

109 Jermain v. Lake Shore & Michigan Southern Ry. Co., 91 N. Y. 483, 2 Keener's Cas. 1411; Coleman v. Columbia Oil Co., 51 Pa. St. 74; and other cases above cited.

110 See post, § 585 et seq., as to effect of omission to register transfers.

111 Boyd v. Conshohocken Wor-

sted Mills, 149 Pa. St. 363; Central Nebraska Nat. Bank v. Wilder, 32 Neb. 454; Hill v. Newichawanick Co., 8 Hun (N. Y.) 459, 71 N. Y. 593; Gemmell v. Davis, 75 Md. 546, 32 Am. St. Rep. 412; Guarantee Co. of North America v. East Rome Town Co., 96 Ga. 511, 51 Am. St. Rep. 150; Armour v. East Rome Town Co., 98 Ga. 458; Hunt v. Laconia & Lakeport St. Ry. Co., 68 N. H. 561; George R. Barse Live Stock Co. v. Range Valley Cattle Co., 16 Utah, 59; Gaty v. Holliday, 8 Mo. App. 118. Where a note and a pledge of

(3) Transfers not made on books of corporation.—Where, for the protection of the corporation, it is expressly provided in its certificates of stock that the shares are not transferrable except on the books of the corporation. 112 the corporation is not bound to look beyond its books, assuming that they have been kept properly, to determine who is entitled to dividends, but it may safely pay them to those persons who appear on the books to be shareholders, and it will be protected in such payment, notwithstanding transfers made before the dividend was declared, but which had not been entered upon its books, and of which it had no notice.113 It is otherwise, however, if it has notice of the transfer. In such a case, if it pays the dividend to the person appearing on its books as owner, it remains liable to the transferee, whether the transfer was absolute or merely as collateral, notwithstanding his omission to have his transfer registered. 114

In paying dividends to a person who appears on the books as the owner of shares, the corporation is not bound to require him to produce his certificate of stock, and his failure to produce it is not sufficient to put the corporation on inquiry, and constitute constructive notice of a transfer of the stock by him, 115 Nor is the corporation put upon inquiry by the fact that the person appearing on the books as owner has represented that his

stock to secure the same were renewed, and a new note given, after a dividend had been declared, it was held that it belonged to the pledgor. Fairbank v. Merchants' Nat. Bank of Chicago, 132 Ill. 120.

112 Post, § 585 et seq., "Transfer." 113 Brisbane v. Delaware, Lackawanna & W. R. Co., 94 N. Y. 204; Cleveland & Mahoning R. Co. v. Robbins, 35 Ohio St. 483; Donnally v. Hearndon, 41 W. Va. 519; Northrop v. Newtown & Bridgeport Turnpike Co., 3 Conn. 544; Bank of Commerce's Appeal, 73 Pa. St. 59; Jones v. Terre Haute & Richmond R. Co., 29 Barb. (N. Y.) 353, 57 N. Y. 196.

114 Robinson v. New Berne Nat. Robbins, 35 Ohio St. 483.

Bank, 95 N. Y. 637, 2 Cum. Cas. 157; Jones v. Terre Haute & Richmond R. Co., 57 N. Y. 196; Boyd v. Conshohocken Worsted Mills, 149 Pa. St. 363; Gemmell v. Davis, 75 Md. 546, 32 Am. St. Rep. 412; Timberlake v. Shippers' Compress Co., 72 Miss. 323; Guarantee Co. of North America v. East Rome Town Co., 96 V. East Rome Town Co., vo Ga. 511,51 Am. St. Rep. 150; Armour v. East Rome Town Co., 98 Ga. 458; Hill v. Atoka Coal & Mining Co. (Mo.) 21 S. W. 508; Central Nebraska Nat. Bank v. Wilder, 32 Neb. 454; Bates v. Androscoggin & Kennebec R. Co., 49 Me. 491.

<sup>115</sup> Brisbane v. Delaware, Lackawanna & W. R. Co., 94 N. Y. 204; Cleveland & Mahoning R. Co. v.

certificate has been lost or destroyed, given a bond of indemnity, and received a new certificate. 116

---(4) Rights of legatees.--A legatee of shares of stock is entitled to all dividends declared after the testator's death, although out of profits earned before, but he is not entitled, unless by express provision in the will, to dividends declared before the testator's death, although not payable until afterwards. Such dividends form part of the corpus of the estate, and go to the executor,117

When the owner of stock dies after a dividend is declared, the dividend is part of his estate, although not payable until after his death, and therefore it does not pass under a clause of his will giving the income of his estate to his widow for life; but a dividend declared after his death, although payable out of profits earned before, will pass as income; instead of going to the executor as a part of the estate. 118 The right to dividends as between a person entitled to the income and profits of stock and the remainderman is considered in a subsequent section.119

- -(5) Interpleader.—In case conflicting claims are made to dividends by the transferrer and the transferee of shares, or by the pledgor and pledgee, the corporation may file a bill of interpleader.120
- (d) Husband and wife.—At common law, shares of stock owned by a married woman, and the right to dividends thereon, belong to the husband if he reduces them to possession, and dividends are reduced to possession by the husband if he receives

legatee of the stock; but he is not entitled to a scrip dividend receq. 283; Brundage v. Brundage, 65 ed by the testator. Brundage Barb. (N. Y.) 397, 1 Thomp. & C. v. Brundage, 65 Barb. (N. Y.) 397, 282, 60 N. Y. 544; In re Kernochan, 104 N. Y. 618; Phelps v. Farmers' & Mechanics' Bank, 26 Conn. 269.

118 In re Kernochan, 104 N. V. 112 Post, § 526.

before a scrip dividend is de- ley v. Pfister, 83 Wis. 64.

116 Brisbane v. Delaware, Lackaclared, the dividend goes to the wanna & W. R. Co., 94 N. Y. 204. legatee of the stock; but he is not

118 In re Kernochan, 104 N. Y.
618; Wiltbank's Appeal, 64 Pa. St.
256, 3 Am. Rep. 585.

120 Cross v. Eureka Lake & Yuba
Canal Co., 73 Cal. 202, 2 Am. St.
Rep. 808; Salisbury Mills v. Towns-Where the owner of stock dies end, 109 Mass. 115. Compare Hinckthem. 121 In most jurisdictions, however, the married woman's acts have changed the common law, and given married women their property free from the control of the husband; and where this is the case, a corporation has no right to pay a husband vidends on shares owned by his wife, unless she authorizes the payment.

The right of a husband to dividends on his wife's stock is governed, in so far as the right of the corporation to pay the same is concerned, not by the law of the state in which they reside, but by the law of the domicile of the corporation. 122

- (e) Other corporations.—Of course a corporation holding stock in another corporation under power conferred by its charter has the same right to dividends as any other stockholder. And the same is true, even when a corporation exceeds its powers in subscribing for or purchasing stock in another corporation. If the contract has been fully executed, the corporation acquires title to the stock, and, as the owner thereof, is entitled to dividends.123
- § 526. Rights of persons entitled to income and profits of shares—(a) In general.—When a person is entitled to the income and profits of shares of stock for life or for a term of years, under a will or gift, there is a conflict of opinion as to his right to dividends. The following summary may be given:
- (1) He is not entitled to share in the profits of the corporation before a dividend is declared.

121 See Brown v. Bokee, 53 Md. 155; Slaymaker v. Bank of Gettysburg, 10 Pa. St. 373; Wells v. Tyler, 5 Fost. (N. H.) 340; Dow v. Gould & Curry Silver Mining Co., 31 Cal. 629; Graham v. First Nat. Bank of Norfolk, 20 Hun (N. Y.) 325, 84 N. Y. 393, 38 Am. Rep. 528; Searing v. Searing, 9 Paige (N. Y.) 283; Burr v. Sherwood, 3 Bradf. (N. Y.) 85; Harcum's Adm'r v. Hudnall, 14 Grat. (Va.) 369.

A husband's receipt of dividends on his wife's stock is not a reduction of the stock to his possession. Burr v. Sherwood, 3 Bradf. (N. Y.)

85.

122 Graham v. First Nat. Bank of Norfolk, 20 Hun (N. Y.) 325, 84 N. Y. 393, 38 Am. Rep. 528,

123 Bigbee & Warrior Packet Co. v. Moore, 121 Ala. 379; Germania Nat. Bank of Orleans v. Case, 99 U. S. Keener's Cas. 1186, 1 Cum. Cas. 948; Holmes & Griggs Mfg. Co. v. Holmes & Wessell Metal Co., 127 N. Y. 252, 24 Am. St. Rep. 448, 1 Keener's Cas. 730, 2 Cum. Cas. 85; Milbank v. New York, Lake Erie & W. R. Co., 64 How. Pr. (N. Y.) 20, 1 Smith's Cas. 963, 1 Cum. Cas. 353.

- (2) He is not entitled to dividends declared before the testator's death.
- (3) He is entitled to dividends declared after the testator's death, if declared out of profits earned since his death.
- (4) Some courts hold that he is entitled to dividends declared after the testator's death, though declared out of profits earned and accumulated by the corporation before his death; but the rule is otherwise in several states.
- (5) He is not entitled to dividends declared out of the capital, or funds representing capital.
- (6) He is entitled to dividends out of profits payable in bonds or certificates of indebtedness.
- (7) He is not entitled to the right to subscribe for new shares on an increase of the capital stock, nor to the proceeds of a sale of such privilege.
- (8) In some states it is held that he is entitled to a stock dividend if he would be entitled to the same dividend if payable in cash, but the rule in other states is to the contrary.
- (9) On his death, his personal representative is entitled to a dividend declared during his lifetime, and it has been held that he is entitled to a dividend declared after his death out of profits earned during his lifetime.

Where shares of stock are given by will or otherwise transferred in trust to pay the income and profits to one person for life or for a term of years, and the principal to another on termination of the life estate or term, or where a fund subject to such a trust is invested by the trustee in shares of stock, difficult questions arise as to the right to dividends on the shares as between the life tenant or tenant for years and the remainderman, or, in other words, as to what dividends constitute "income" or "profits," and go to the life beneficiary or tenant for years, and what constitute an addition to the principal, and go to the remainderman. On some of these questions the decisions are in direct conflict.

(b) Before declaration of dividend.—The terms "income" and "profits" in such a bequest or gift certainly do not include profits in the hands of the corporation before any dividend has

been declared, for until a dividend is declared, no stockholder has any legal right to profits earned by the corporation. 124

- (c) After dividend has been declared—(1) Dividends declared before creation of the trust.—Under a bequest or gift of the income and profits of shares of stock for life or years, the beneficiary is not entitled to dividends declared before, although not payable until after, the testator's death or the time of the gift. Such a dividend is a debt due from the corporation, and passes to the executor as a part of the estate. "As soon as the profits on shares of stock are ascertained and declared," said the New York court in such a case, "they cease to be the property of the company, and the owner of the shares becomes entitled to the dividend. It at once forms part of his estate. The fact that they are made payable at a future time is immaterial. dividend to which the life tenant may be entitled as income, can only be that which the company declares after that relation is acquired. In this case the dividend represented profits or income, but had become a debt before the will took effect."125
- -- (2) Dividends declared after the creation of the trust. When the owner of shares of stock makes a bequest or gift of the income and profits to a person for life, there can be no doubt that all ordinary cash dividends 126 declared after creation of the trust will belong to the life tenant as income or profits, if they are declared out of profits earned by the corporation since the testator's death. There is probably no decision in conflict with this proposition. If there is, it certainly cannot be sustained. 127

Some of the courts have gone further than this, and have held that all cash dividends out of profits, declared after the testator's death, go to the life tenant, although they are payable out of profits earned by the corporation before his death, and al-

<sup>124</sup> Ante, § 517(b)

<sup>126</sup> As to stock dividends, see infra, this section, (c) (6). As to infra, this section, (c) (6). As to 650; Davis v. Jackson, 152 Mass. dividends payable in bonds, scrip, 58. 23 Am. St. Rep. 801; and cases certificates of indebtedness, etc., cited in the notes following. see infra, this section, (c) (4).

<sup>127</sup> Earp's Appeal, 28 Pa. St. 368; 125 In re Kernochan, 104 N. Y. Estate of Smith, 140 Pa. St. 344. 23 Am. St. Rep. 237; Van Doren v. Olden, 19 N. J. Eq. 176, 97 Am. Dec.

though it may be, not an ordinary dividend, but an extraordinary or unusual dividend, payable out of profits which had been allowed to accumulate for a number of years before the testator's death.128

Other courts have taken a different view. In Pennsylvania, for example, it is held that the life tenant is entitled to all dividends declared out of profits earned after the testator's death, but not to dividends out of profits which accumulated during his lifetime. 129 In a late case it was said by Judge Clark:

Me. 570, 46 Am. Rep. 428; Millen v. Guerrard, 67 Ga. 284, 44 Am. Rep. 720; Reed v. Head, 6 Allen (Mass.) 174; Woodruff's Estate, 1 Tuck. (N. Y.) 58; Clarkson v. Clarkson, 18 Barb. (N. Y.) 646; Simpson v. Moore, 30 Barb. (N. Y.) 637; Goldsmith v. Swift, 25 Hun (N. Y.) 201; Riggs v. Cragg, 26 Hun (N. Y.) 89; King v. Follett, 3 Vt. 385; In re Kernochan, 104 N.

In Richardson v. Richardson, 75 Me. 570, 46 Am. Rep. 428, it was held that, where a corporation declares a dividend on its stock payable in money, the stockholder at the time, whether a life tenant or a remainderman, is entitled to the whole dividend, irrespective of its source, amount, or the length of time in which it was earned.

In Gilkey v. Paine, 80 Me. 319, it was held that one entitled to the "net annual income" of stock was to all dividends and entitled bonuses distributed which represented surplus earnings.

In New York, extraordinary dividends belong to the person holding a life interest in the stock on which such dividends are earned. Woodruff's Estate, 1 Tuck. (N. Y.)

In other words, net earnings which are allowed to accumulate after the creation of the trust do not, for that reason, become principal. They remain income, and go to the life beneficiary when finally divided as dividends. Lord Brooks, 52 N. H. 72. "If it be con-

128 Richardson v. Richardson, 75 ceded," said the court in this case, "that the net earnings of the bank remain the property of the bank as fully as its other property till the directors declare a dividend, and that the tenant for life has no title to them prior to the dividend being declared, still, their nature remains the same all the time; and when they are divided, the tenant for life is just as much entitled to them as though they had been divided the moment they were Their source is not chanearned. ged by the delay in distribution. It may often be expedient for the directors to retain a portion of the net earnings as a reserve fund to meet contingencies. This reserve fund may often be spoken of as 'capital,' irrespective of the source whence it is derived. But, when the necessity for the reservation ceases, and the reserve fund is divided among the shareholders, the question whether it is income or capital depends on its origin. If it was originally taken from the net earnings, it belongs to the tenant for life, if distributed in her lifetime.'

See, also, Thomas v. Gregg, 78 Md. 545; McLouth v. Hunt, 154 N. Y. 179, affirming 92 Hun, 607; Lowry v. Farmers' Loan & Trust Co., 56 App. Div. (N. Y.) 408, reversing 30 Misc. Rep. 334.

129 Estate of Smith, 140 Pa. St.
 344, 23 Am. St. Rep. 237; Earp's
 Appeal, 28 Pa. St. 368; Wiltbank's
 Appeal, 64 Pa. St. 256, 3 Am. Rep.
 585; Biddle's Appeal, 99 Pa. St.

"It is well settled in this state that, when the stock of a corporation is by the will of a decedent given in trust, the income thereof for the use of a beneficiary for life, with remainder over, the surplus profits, which have accumulated in the lifetime of the testator but which are not divided until after death, belong to the corpus of his estate; while the dividends of earnings made after his death are income, and are payable to the life tenant."130 In an earlier case it was said: "Where the profits of a manufacturing or banking corporation have been accumulating for many years until the market value of the stock is more than double its original price, and the owner dies, directing the 'income' of his estate to be applied to particular objects for limited periods, these extraordinary accumulations are as much a part of his capital as any other portion of his estate, and must, therefore, be regarded as forming a part of the principal from which the future income is to arise."131

This doctrine is also recognized in New Jersey. It was there held that, under a will bequeathing the income of a fund subsequently invested in shares of stock to a life tenant, and the principal to a remainderman, undivided earnings laid up by the corporation, as well as the par value of the shares, should be kept intact for the benefit of the remainderman, while the life tenant is entitled to the income on the undivided earnings. "Where trust funds," said Chancellor Zabriskie, "of which the income, interest, or profits are given to one person for life, and the principal bequeathed over upon the death of the life tenant, are invested either by the trustee, or at the death of the testator. in stock or shares of an incorporated company, the value of which consists in part of an accumulated surplus or undivided earnings laid up by the company, as is frequently the case, such additional value is part of the capital; that this, as well as the par value of the shares, must be kept by the trustees intact for the benefit of the remainderman; but the earnings on such capital, as well

<sup>278.</sup> Compare Estate of Oliver, 180 Estate of Smith, 140 Pa. St. 136 Pa. St. 43, 20 Am. St. Rep. 894. 344, 23 Am. St. Rep. 237. 181 Earp's Appeal, 28 Pa. St. 368.

as upon the par value of the shares, belongs to the life tenant."132

According to this doctrine, if a dividend is declared out of profits earned partly before and partly after the testator's death, it is apportioned between the life tenant and the remainderman. 133

In England the rule was at one time that ordinary or usual dividends declared after a testator's death, whether out of profits earned before or after his death, are income, and not principal, and go to the tenant for life of shares, but that extraordinary or unusual dividends form part of the corpus of the estate, and go to the remainderman; 134 but there are late cases in which the life tenant has been held to be entitled to an extraordinary cash dividend.135

-Intention of the testator.—In all cases, when a question arises as to whether certain dividends go to the life beneficiary of shares, the determination of the question depends primarily upon the intention of the testator or donor, and the intention, when once ascertained from the language of the will or other instrument, and the surrounding circumstances, must be given effect. 136

132 Van Doren v. Olden, 19 N. J. Eq. 176, 97 Am. Dec. 650. See, also, Lang's Ex'r v. Lang, 56 N. J. Eq. 603; Ashurst v. Field's Adm'r, 26 N. J. Eq. 11; Pratt v. Douglas, 38 N. J. Eq. 516, 541.

Under a will bequeathing the income of a fund subsequently invested in shares of stock to a life tenant and the principal to a remainderman, an extra dividend belongs to the life tenant, where it is no part of the earnings which had been carried to account of accumulated profits before the testator's death. Van Doren v. Olden, 19 N. J. Eq. 176, 97 Am. Dec. 650.

In a late New Jersey case it was said: "I understand this principle or rule to mean that the actual value of the shares at the time of the death of the testator, so far as the same can be ascertained, is the

capital or principal intended by the testator for the remaindermen. This value at testator's death is evidenced in part by the book assets, including the accumulated surplus account standing on the books at that time, and in cases where the stock has a market value (as in Earp's Appeal, 28 Pa. St. 368), this also is evidence of value." Lang's Ex'r v. Lang, 56 N. J. Eq. 603. And see Smith's Estate, 140 Pa. St. 344.

133 Earp's Appeal, 28 Pa. St. 368. 134 Bates v. Mackinley, 31 Beav. 280. See In re Hopkins' Trusts, L. R. 18 Eq. 696, 30 Law T. (N. S.) 627; Barclay v. Wainewright, 14 Ves. 66; Paris v. Paris, 10 Ves. 185.

135 See Ellis v. Barfield, 64 Law T. (N. S.) 625, and Sugden v. Alsbury, 45 Ch. Div. 237.

136 Where a will gave a person

(3) Dividends declared out of capital.—As a rule, dividends declared by a corporation out of its capital, or funds representing capital, as where it sells a portion of the property or franchises in which its capital is invested, and distributes the proceeds, are not income or profits, and do not go to the life beneficiary, but are a part of the principal which must be preserved for the remainderman. 137

For example, if a city takes from a corporation, in the exercise of the power of eminent domain, property in which its capital has been invested, the money paid as compensation represents capital, and not profits, and if it is distributed by the corporation

the income for life of shares of tain supposed losses, and on the stock in a corporation, the only income from which was from the sale of lands received by the corporation in payment of work upon railroads constructed by it, it was held that dividends paid by the corporation out of the proceeds of such sales should be treated as income, and went to the life beneficiary, and not to the remainderman, such, in the opinion of the court, being clearly the intention

court, being clearly the intention of the testator. In re James, 146 N. Y. 78, 48 Am. St. Rep. 774.

127 Vinton's Appeal, 99 Pa. St. 434, 44 Am. Rep. 116; Gifford v. Thompson, 115 Mass. 478; Heard v. Eldredge, 109 Mass. 258, 12 Am. Rep. 687; Wheeler v. Perry, 18 N. H. 307; Walker v. Walker, 68 N. H. 407; In re James, 78 Hun, 121, 146 N. Y. 78; Matter of Skillman, 24 Abb. N. C. (N. Y.) 41, 9 N. Y. Supp. 469. Supp. 469.

In Gilkey v. Paine, 80 Me. 319, it was held that one who is entitled to the "net annual income" of stock, although entitled to all dividends and bonuses distributed which represent surplus earnings, is not entitled to capital stock purchased by the corporation on credit of its bonds, although such stock, when distributed, is charged to the profit and loss account.

Where a corporation, duly authorized, reduced the par value of thorized, reduced the par value of evidence to the contrary. Walker its shares in consequence of cer- v. Walker, 68 N. H. 407.

recovery of the sums supposed to have been lost issued additional stock to its stockholders, it was held that one having a right for life to the income and profits of certain shares under a will was not entitled to an unconditional certificate of the new dividend stock, since the amount of the recovered debt could not be regarded as income or profits on the shares of stock. Parker v. Mason. 8 R. I. 427.

Where trustees of a corporation exchanged stock, on the consolidation of the corporation with another, for stock in the consolidated company, and received additional certificates to represent the difference in value of the old stock over the new, the additional stock was held to be "capital," and not "income," within a bequest of the income of the original stock. Clarkson v. Clarkson, 18 Barb. (N. Y.) 646.

Money or stock received and held by the trustee should be regarded capital unless the evidence shows that it is income. Peirce v. Burroughs, 58 N. H. 302; Law v. Alley, 67 N. H. 93.

But since dividends are properly payable only out of profits, dividends declared and paid are presumed to be income unless there is

as a dividend, it does not go to a person who is entitled merely to the income and profits of shares. 138

And where a corporation ceases business and sells all its property, with a view to distribution among its stockholders, or when a corporation is dissolved, and its assets so distributed, the dividend goes to the remainderman, and not to the life tenant of shares. 139 Where a corporation, in whose stock a trust fund was invested, sold its assets and property, and voted to pay a dividend in cash to its stockholders on surrender of their certificates, the assets consisting at the time in part of capital and in part of undivided earnings, it was held that the entire amount received by the trustee was capital, and not income, and belonged to the remainderman, and not to the life beneficiary of In such a case, however, according to the better the fund.140 opinion, there should be an apportionment, so much of the dividends as represents profits going to the life beneficiary, and so much as represents capital going to the remainderman.\*

This rule does not apply where the nature of a corporation is such that its ordinary business is to sell property in which its capital is invested, and distribute the proceeds among its stockholders. In a Massachusetts case, for example, it was held that a legatee entitled to the income for life from stock in a company deriving its profits from the improvement and sale of land was entitled to the ordinary dividends declared thereon, although they in reality consisted of a portion of the capital stock.<sup>141</sup>

258, 12 Am. Rep. 687.

139 Gifford v. Thompson, 115 Mass. 478; Wheeler v. Perry, 18 N.

140 Gifford v. Thompson, 115 Mass. 478.

\* Cobb v. Fant, 36 S. C. 1; In re Rogers, 161 N. Y. 108, affirming 22 App. Div. 428.

As to apportionment between life beneficiary and remainderman on distribution of assets including accumulated profits, on dissolution of corporation, see In re Rogers, 161 N. Y. 108, affirming 22 App. Div.

138 Heard v. Eldredge, 109 Mass. ant for life and remainderman 8, 12 Am. Rep. 687. when, in the execution of a trust, 139 Gifford v. Thompson, 115 stock is sold *cum* dividend, see Bulkeley v. Stephens [1896] 2 Ch.

> Where the capital stock of a corporation was reduced by returning half of it to the stockholders, with a premium of forty per cent. to be paid out of surplus, it was held that the premium paid out of surplus was income, and belonged to the life beneficiary of shares. In re Warren's Estate, 33 N. Y. St. Rep. 584, 11 N. Y. Supp. 787.
>
> 141 Reed v. Head, 6 Allen (Mass.)

28. 174. And see In re James, 78 Hun, As to apportionment between ten- 121, 146 N. Y. 78.

There was a like decision where a manufacturing corporation sold patent rights in which a part of its capital had been invested, and castings, and declared a dividend in cash out of the proceeds.142

- —(4) Proceeds of shares sold.—When a trust fund, the proceeds or income of which is to be paid to one person for life, with remainder to another, is invested in shares of stock, and the stock is sold, the proceeds of the sale are principal, and do not go to the life beneficiary, except in so far as they represent accumulated profits.\*
- ---(5) Dividends in bonds or certificates of indebtedness.-Dividends declared out of profits go to the person entitled to the income and profits of shares, although they are paid, not in cash, but in bonds of the company or certificates of indebtedness.143
- -(6) Right to subscribe for shares, etc., and proceeds of sale thereof.—Where the capital stock of a corporation is increased under legislative authority, the privilege or right which the shareholders have to subscribe for the new shares is appurtenant to the original stock, and does not belong to the person entitled to the income of the shares. And, according to

Rep. 774.

\* In re Kernochan, 104 N. Y. 618. As to the apportionment in such a case, the stock being sold cum dividend, see Bulkeley v. Stephens [1896] 2 Ch. 241.

143 Millen v. Guerrard, 67 Ga. 284, 44 Am. Rep. 720.

144 Hite v. Hite, 93 Ky. 257, 40 Am. St. Rep. 189; In re Kernochan, 104 N. Y. 618; Thomson's Estate, 153 Pa. St. 332. Compare, however. Bushee v. Freeborn, 11 R. I. 149, and cases cited below.

Where a corporation, having a surplus of earnings, increased its stock, and permitted the stockholders to subscribe at par for as many

142 Harvard College v. Amory, 9 shares as they held of the old stock, Pick. (Mass.) 446. See, also, In and an estate holding one hundred re James, 146 N. Y. 78, 48 Am. St. shares sold sixty of the options, with which it purchased forty new shares, it was held that these were capital, and not income, under a will bequeathing the stock subject to a life use of the income. Moss's Appeal, 83 Pa. St. 264, 24 Am. Rep. 164.

> The right given to stockholders to subscribe at par for new shares issued by the corporation, and which are worth more than par, is to be regarded as capital, and not as income, so as to belong to the life beneficiary, unless the evidence shows that the new shares represent earnings. Peirce v. Burroughs, 58 N. H. 302; Law v. Alley, 67 N. H. 93; Walker v. Walker, 68 N. H.

the weight of authority, if such right and privilege is sold by a trustee who holds shares on which a person is entitled to the income for life, the proceeds of the sales go, not to the life tenant, but to the remainderman. 145

The same is true of other options or privileges which are appurtenant to the stock,—as an option or privilege to subscribe for or purchase stock or bonds in another corporation, or an option or privilege to subscribe for bonds in another corporation, stock of which is to be given to the subscribers as a bonus.\*

-(7) Stock dividends.—In some jurisdictions, no distinction at all is made between dividends payable in cash and dividends payable in stock or scrip entitling the holder to stock, so far as the respective rights of life beneficiary and remainderman are concerned; but it is held that a stock dividend declared on shares out of profits belongs to the person entitled to the income or profits, if, under the same circumstances, he would be entitled to a cash dividend. Thus, in Pennsylvania, where it is held, as we have seen, that a legatee of the income and profits of shares is entitled to dividends declared out of profits earned after the testator's death, but not to dividends out of profits which had accumulated before his death, it is held that this rule applies, "no matter whether the dividend be in cash or scrip or stock."146

145 Atkins v. Albree, 12 Allen (Mass.) 359; Hite v. Hite, 93 Ky. 257, 40 Am. St. Rep. 189; Brinley v. Grou, 50 Conn. 66, 47 Am. Rep. 618; Biddle's Appeal, 99 Pa. St. 278; Moss' Appeal, 83 Pa. St. 264, 24 Am. St. Rep. 164; Greene v. Smith, 17 R. I. 28; Walker v. Walker, 68 N. H. 407.

Where a corporation increased its capital stock by offering to stockholders the option of subscribing at par to the stock, in the proportion of one share for every two shares held, the proceeds of a sale of an option by one holding stock in trust to collect the income for the use of another for life are to be accounted capital, and not in-come, in so far as they relate to the 28 Pa. St. 368; Wiltbank's Appeal,

beneficiary. Biddle's Appeal, Pa. St. 278.

But in Wiltbank's Appeal, 64 Pa. St. 256, 3 Am. Rep. 585, it was held that, where a corporation ordered a distribution of increased stock to stockholders on the payment of so much per share, and one holding stock in trust to pay the income to another for life sold the privilege to subscribe, the proceeds of sale should be regarded as income, and not as capital, where there was no serious diminution in the value of old stock caused by the new issue. \* In re Kernochan, 104 N. Y. 618;

Thomson's Estate, 153 Pa. St. 332. 146 Per Judge Clark, in Estate of Smith, 140 Pa. St. 344, 23 Am. St.

"Where a corporation," said Judge Paxson in a Pennsylvania case, "having actually made profits, proceeds to distribute such profits among the stockholders, the tenant for life would be entitled to receive them, and this without regard to the form of the Equity, which disregards form and grasps the substance, would award the thing distributed, whether stock or moneys, to whomsoever was entitled to the profits."147

The doctrine that a stock dividend passes to the beneficiary under a gift or bequest of the income and profits of shares has also been recognized in Kentucky, 148 New York, 149 New Jersey,\* Maryland,150 and Tennessee.†

In some jurisdictions, this doctrine is not recognized. Massachusetts, for example, it is held that a stock dividend on shares, although it may be declared out of profits earned after the death of the testator, becomes a part of the corpus of the estate, to be preserved for the remainderman, and does not go to the life beneficiary as income or profits. 151 This doctrine

64 Pa. St. 256, 3 Am. Rep. 585; Moss' Appeal, 83 Pa. St. 264, 24 Am. Rep. 164; Vinton's Appeal, 99 Pa. St. 434, 44 Am. Rep. 116; Appeal of Philadelphia Trust, Safe-Deposit & Insurance Co. (Pa.) 16 Atl. 734; Turpin's Estate, 21 Wkly. Notes Cas. (Pa.) 542.

147 Moss' Appeal, 83 Pa. St. 264,

24 Am. Rep. 164.

148 Hite v. Hite, 93 Ky. 257, 40 Am. St. Rep. 189.

149 Goldsmith v. Swift, 25 Hun (N. Y.) 201; Riggs v. Cragg, 26 Hun (N. Y.) 89; Clarkson v. Clarkson, 18 Barb. (N. Y.) 646; Simpson v. Moore, 30 Barb. (N. Y.) 637; Mc-Louth v. Hunt, 154 N. Y. 179, affirming 92 Hun, 607; Lowry v. Farmers' Loan & Trust Co., 56 App. Div. (N. Y.) 408, reversing 30 Misc. Rep. 334.

While a stock dividend representing earnings belongs to the income, and not to the principal, of a trust estate, as between the tenant for life and remainderman, yet, where the additional shares are issued only for the purpose of equalizing the value of the interests of stockholders in two corporations about to be consolidated, they belong to the principal, and not to the income. Goldsmith v. Swift, 25 Hun (N. Y.) 201.

Where an extra dividend of an accumulated surplus in a bank was declared payable either in new stock or money, and a trustee under a will, who had invested in the stock of the bank, took the stock, it was held that the payment was a dividend, and belonged to the life interest in the trust fund, but that so much should be retained out of the dividend and added to the fund as would make the market value of the stock equal to its market value at the time of the original investment by the trustee, so that the amount invested should not be diminished. Simpson v. Moore, 30 Barb. (N. Y.) 637.

\* Ashhurst v. Field's Adm'r, 26 N. J. Eg. 1.

150 Thomas v. Gregg, 78 Md. 545. 44 Am. St. Rep. 310.

† Pritchett v. Nashville Trust Co., 96 Tenn. 472.

151 Minot v. Paine, 99 Mass. 101.

proceeds on the ground that since, in the absence of any restraining statute, a corporation may treat and deal with the money earned by it either as an increase of its property, or as the profits of its business, so long as the corporation holds it as part of the corporate property, it is capital of the corporation, and the interest therein represented by each share of stock is capital, and not income of that share.<sup>152</sup>

The Massachusetts doctrine has also been adopted or recognized in Connecticut, Maine, and Rhode Island, by the supreme court of the United States, by the appellate court in Illinois, and by the supreme court of the District of Columbia.

This also seems to be the rule in England. "When a testator

96 Am. Dec. 705; Daland v. Williams, 101 Mass. 571; Leland v. Hayden, 102 Mass. 542; Rand v. Hubbell, 115 Mass. 461, 15 Am. Rep. 121; Davis v. Jackson, 152 Mass. 58, 23 Am. St. Rep. 801; Atkins v. Albree, 12 Allen (Mass.) 359.

152 Rand v. Hubbell, 115 Mass.

461, 15 Am. Rep. 121.

153 Brinley v. Grou, 50 Conn. 66, 47 Am. Rep. 618; Hotchkiss v. Brainerd Quarry Co., 58 Conn. 120; Spooner v. Phillips, 62 Conn. 62; Mills v. Britton, 64 Conn. 4.

In Spooner v. Phillips, 62 Conn. 62, it was held that, where an association increases its capital stock to represent profits actually invested in extending its business and increasing the value of its plant, and apportions new shares pro rata among the existing shareholders, the new shares represent capital, and not "income" or "dividends," and do not pass by a gift of the original shares by deed of trust "to and for the use of" another, and "to pay over to her the dividends and income thereof" during her life, and on her decease "to reconvey and transfer said stock" to the donor.

<sup>154</sup> See Richardson v. Richardson,75 Me. 570, 46 Am. Rep. 428.

155 Petition of Brown, 14 R. I.
 371, 51 Am. Rep. 397; Greene v.

Smith, 17 R. I. 28. Compare Bushee v. Freeborn, 11 R. I. 149.

<sup>156</sup> Gibbons v. Mahon, 136 U. S. 549.

In this case, a testatrix bequeathed two hundred and eighty shares of stock in a gaslight company in trust to pay dividends, "without diminution of principal," to her daughter for life. The company having, from its earnings, doubled its original plant, issued, after the death of testatrix, additional shares of stock, representing this increase in the capital, and divided them among the stockholders in proportion to the original stock owned by them. The beneficiary claiming these additional shares absolutely, on the ground that they represented the profits or earnings of the original shares, and were, in effect, dividends, it was held that they were in no sense dividends, and that it was the duty of the trustee to hold them, together with the original shares, for the benefit of the remainderman, paying only the dividends upon the whole number to the life legatee.

<sup>157</sup> Waterman v. Alden, 42 Ill. App. 294.

158 Gibbons v. Mahon, 4 Mackey (D. C.) 130, 54 Am. Rep. 262, affirmed in 136 U. S. 549, note 156, supra.

or settlor," it was there said, "directs or permits the subject of his disposition to remain as shares or stocks in a company which has the power either of distributing its profits as dividend or of converting them into capital, and the company validly exercises this power, such exercise of its power is binding on all persons interested under the testator or settlor in the shares, and consequently what is paid by the company as dividend goes to the tenant for life, and what is paid by the company to the shareholder as capital, or appropriated as an increase of the capital stock in the concern, inures to the benefit of all who are interested in the capital."

—Whether a dividend is a stock dividend.—Where a distribution is made by a corporation among its shareholders of money earned by the corporation, the question whether such distribution is an apportionment of additional stock, which will go to the remainderman under the Massachusetts rule, or a division of profits, which will go to the life beneficiary of the income and profits, depends upon the substance and intent of the action of the corporation, as shown by its vote. The question has arisen in several Massachusetts cases.

In one case, where a trust fund of which the income was payable to a person for life was invested in the stock of a corporation which had no authority to make stock dividends, and the corporation, having an undivided surplus, voted to increase its capital stock, declared a dividend, and authorized such dividend to be received in payment of shares of the new issue, it was held that the dividend was in effect a stock dividend, and the life tenant was not entitled thereto.<sup>161</sup>

In another case, where a corporation passed a vote to increase

159 Fry, J., in Bouch v. Sproule, 12 App. Cas. 385, 397. And see In re Barton's Trust, L. R. 5 Eq. 238. 160 Rand v. Hubbell, 115 Mass. 461, 15 Am. Rep. 121.

Where a corporation, being unable to pay arrears of dividends on Mill cumulative preferred stock, compromised with the holders, reduc-

ing the amount of the dividend one-half, and issuing double the amount of his stock to each stockholder, it was held that the new stock went to the remainderman, and not to the life beneficiary. Mills v. Britton, 64 Conn. 4.

161 Daland v. Williams, 101 Mass.

its capital stock, and the board of directors, in pursuance thereof. declared that a dividend in cash should be payable to each stockholder, but that it should be applied by him in payment of the new shares, and directed the treasurer of the corporation to issue certificates for the new shares to stockholders only, and the treasurer gave to each stockholder a check for his share of the dividend, which checks were surrendered by the stockholders in exchange for new shares, and destroyed, it was held that the dividend was in effect a stock dividend, and that a person entitled to the income of shares for life had no right thereto. 162

In a later case, however, where a dividend payable in cash was declared out of the profits of a corporation, it was held to be income as between life tenant and remainderman, although permanent improvements to an equal amount had previously been made by the corporation, and it was just sufficient to pay for a voted increase of the capital stock for which the stockholders were at liberty to subscribe in proportion to their shares 163

(d) Rights on death of life tenant.—Upon the death of a person entitled to the income and profits of shares of stock for life, his executor or administrator is clearly entitled to dividends declared during his lifetime.164

It would seem equally clear that all dividends declared after his death, although declared out of profits earned by the corporation during his life, would go to the remainderman. 165 There are decisions, however, to the contrary. In a Massachusetts case, it was held that a bequest of the income of shares in a corporation to the testator's widow for life, for her own support and the education of her children, included a dividend declared thereon after her death for a period which expired during her

<sup>162</sup> Rand v. Hubbell, 115 Mass. 461, 15 Am. Rep. 121.

<sup>&</sup>lt;sup>163</sup> Davis v. Jackson, 152 Mass. 58, 23 Am. St. Rep. 801.

<sup>164</sup> Ante, § 517(c).

<sup>165</sup> Ante, § 517(b).

<sup>818,</sup> it was held that, if the life beneficiary dies before a dividend is declared, the dividend, when declared, is not to be apportioned between his estate and the remainderman, unless the will or other instrument creating the trust clear-In Mann v. Anderson, 106 Ga. ly shows such an intention.

life, although the shares still stood in the name of the testator's estate. 166

And in a South Carolina case, where a donee, to whom the dividends on certain stock were given for life, payable semi-annually, died before a semiannual dividend was declared, it was held that the dividend, when declared, should be apportioned, and the amount which had accrued at the donee's death should be paid to his executor.<sup>167</sup>

§ 527. Remedies of stockholders to recover dividends—(a) In general.—Before a dividend has been declared, assumpsit will not lie by a stockholder against the corporation to recover a share of the profits, but he may sue in equity to compel declaration of a dividend, if the directors in bad faith or unreasonably refuse to declare one. Mandamus will not lie.

After a dividend has been declared, any stockholder, after a demand, may maintain assumpsit against the corporation to recover his share, or, perhaps, he may sue in equity. Mandamus will not lie.

He cannot sue another person whom the corporation has recognized as a stockholder, and to whom it has paid the dividend.

Nor, as a rule, can he sue an officer of the corporation for refusal to pay him his dividend.

He can set off the dividend against a debt due from him to the corporation.

He is entitled to recover interest from the time of a demand upon the corporation, and its refusal to pay.

The statute of limitations runs against an action for a dividend from the time when it is payable; if payable on demand, from the time of a demand and refusal.

(b) Remedies before a dividend has been declared.—As was explained in a former section, until a dividend has been declared by the directors, the stockholders have no legal right or title to any part of the assets of the corporation, although there may be surplus profits out of which a dividend might lawfully be declared; nor is there any indebtedness to them on the part of the

188 Johnson v. Bridgewater Mfg. 167 Ex parte Rutledge, 1 Harp. Co., 14 Gray (Mass.) 274. Eq. (S. C.) 65, 14 Am. Dec. 696.

corporation which will sustain an action by them against the corporation to recover what they would be entitled to receive if a dividend should be declared. 168 The only judicial remedy of the stockholders against the corporation in such a case is by a suit in equity to compel the directors to declare a dividend, and, as we have seen, they cannot maintain such a suit unless the directors have abused their discretion in refusing to declare a dividend by acting in bad faith or unreasonably. 169

The rule that stockholders cannot sue for a dividend until it has been declared by the directors may be changed by express provision in the charter of the corporation. 170 But it cannot be changed by mere agreement between the stockholders.<sup>171</sup>

Mandamus will not lie to compel directors to declare a dividend, but the only remedy, if there is any at all, is in equity.<sup>172</sup>

(c) Remedies after dividend has been declared—(1) Action at law against the corporation.—When the directors of a corporation lawfully declare a dividend, the effect, as we have seen, is to create the relation of debtor and creditor between the corporation and each stockholder for his proportion of the dividend, and if the corporation refuses to pay any stockholder his share, and the dividend is payable in cash, he may recover the same in an action of assumpsit on the common count for money had and received, or in an action of special assumpsit. 173 "After a divi-

168 Phelps v. Farmers' & Mechancs' Bank, 26 Conn. 269; Hyatt v. Allen, 56 N. Y. 553, 15 Am. Rep. 449; Beveridge v. New York Elevated R. Co., 112 N. Y. 1; Goodwin v. Hardy, 57 Me. 143, 99 Am. Dec. 758; Lockhart v. Van Alstyne, 31 Mich. 76, 18 Am. Box. 156, 2 31 Mich. 76, 18 Am. Rep. 156, 2 Keener's Cas. 1354; Williston v. Michigan Southern & Northern Indiana R. Co., 13 Allen (Mass.) 400; American Wire Nail Co. v. York Iron Mine, 24 Jones & S. (N. Y.) 236; ante, § 517(f).

170 In State v. Louisiana Bank, 5 Mart. (N. S.; La.) 327, it was held that, where the charter of a cor-

to a semiannual dividend as a matter of right, they may sue the corporation therefor at the end of each semiannual dividend period. 171 An action for a dividend cannot be maintained where no dividend has been declared, although the stockholders may have agreed that one should be declared. American Wire Nail Co. v. Gedge, 96 Ky. 513.

172 Rex v. Bank of England, 2 Barn. & Ald. 620, 2 Keener's Cas. 1416, 2 Cum. Cas. 218.

173 In re Severn & Wye & Severn Bridge Ry. Co., 74 Law T. (N. S.) 219, 1 Smith's Cas. 322, 2 Keener's Cas. 1342; Ellis v. Essex Merrimack Bridge, 2 Pick. (Mass.) 243; poration entitles the stockholders Hill v. Atoka Coal & Mining Co.

dend is declared, all community of interest in relation to such dividend, as between the stockholders themselves and between the stockholders and the corporation, is at an end. The right of a party to whom the dividend is payable is recognized as a separate and independent right, which may be enforced as against the corporation. \* \* \* The dividend, from the time that it is declared, becomes a debt due from the corporation to the individual stockholder, for the recovery of which, after demand of payment, an action at law may be maintained.;;174

Such an action may be maintained, not only by stockholders who have been recognized by the corporation as entitled to share in the dividend, but also by those who have been wrongfully denied the right to share therein, for the law imposes upon a corporation the duty to distribute all dividends which may be declared from time to time ratably on all of its capital stock, and from this duty the law implies a promise on the part of the corporation to each stockholder. 175

In order that an action of assumpsit may be maintained, there must have been a demand upon the corporation for payment of the dividend, 176 unless the corporation has rendered a demand

(Mo.) 21 S. W. 508; Jackson's Mining Co. (Mo.) 21 S. W. 508; Adm'r v. Newark Plankroad Co., Southwestern, Arkansas & I. T. Ry. 31 N. J. Law, 277, 2 Cum. Cas. 201, 2 Keener's Cas. 1418; West Chester & Philadelphia R. Co. v. Jackson, 77 Pa. St. 321; King v. Paterson & Hudson River R. Co., 29 N. J. Law, 82, 504, 2 Keener's Cas. 1330; Hall v. Rose Hill & Evanston Road Co., 70 Ill. 673; In re Le Blanc, 14 Hun (N. Y.) 8, 75 N. Y. 598; Kane v. Bloodgood, 7 Johns. Ch. (N. Y.) 90; Chaffee v. Rutland R. Co., 55 Vt. 110; Southwestern, Arkansas & I. T. Ry. Co. v. Martin, 57 Ark. 355; ante, § 517(c).

174 King v. Paterson & Hudson River R. Co., 29 N. J. Law, 82, 504, 2 Keener's Cas. 1330.

175 Jackson's Adm'r v. Newark Plankroad Co., 31 N. J. Law, 277, 2 Cum. Cas. 201, 2 Keener's Cas. 1418.

Co. v. Martin, 57 Ark. 355; and other cases cited in note 173, su-

176 State v. Baltimore & Ohio R. Co., 6 Gill (Md.) 363; Bank of Louisville v. Gray, 84 Ky. 565; Hagar v. Union Nat. Bank, 63 Me. 509; Scott v. Central Railroad & Banking Co. of Georgia, 52 Barb. (N. Y.) 45.

Where a bank sued a stockholder on a note, and attached his shares of stock pending the action, and demand was made for payment of a dividend declared upon the attached shares, and refused, it was held that the stockholder, after settling the suit, could not maintain an action for the dividend Cum. Cas. 201, 2 Keener's Cas. 1418. without renewing his demand. Ha-See, also, Hill v. Atoka Coal & gar v. Union Nat. Bank, 63 Me. 509. unnecessary by refusing to recognize the plaintiff as a share-holder.<sup>177</sup>

To sustain an action on the common counts for money had and received, it is necessary that a dividend shall have been declared payable out of money in the hands of the company. In a Maryland case, a dividend was declared, and was directed to be paid to the smaller stockholders in cash, and to the others partly in stock and partly in money, the company not being in funds to the full amount of the dividend. One of the latter class of stockholders refused to take payment to any extent in stock, and sued for money had and received. It was held that the action could not be maintained.<sup>178</sup>

Payment of dividends by a corporation to a person who is not entitled to them does not release the corporation from liability. It remains liable to the person entitled to receive them.<sup>179</sup>

—(2) Action by transferee.—Where shares of stock are transferable only on the books of the corporation, a transferee, so long as the transfer is unregistered, has merely an equitable title, and at common law he cannot maintain an action against the corporation to recover dividends. His remedy is in equity, or by an action at law in the name of the transferrer. Such an action may be maintained in his name, however, where by statute an assignee of a chose in action may sue at law in his own name. 181

When a corporation wrongfully refuses to recognize the right of a transferee of shares to a dividend thereon, he may sue therefor without first bringing an action in equity to compel a trans-

<sup>177</sup> Robinson v. National Bank of New Berne, 95 N. Y. 637, 2 Cum. Cas. 157.

<sup>178</sup> State v. Baltimore & Ohio R. Co., 6 Gill (Md.) 363. As to this case, see Jackson's Adm'r v. Newark Plankroad Co., 31 N. J. Law, 277, 2 Keener's Cas. 1418, 2 Cum. Cas. 201.

<sup>&</sup>lt;sup>179</sup> St. Romes v. Levee Steam Cotton Press, 20 La. Ann. 381, and other cases above cited.

<sup>&</sup>lt;sup>180</sup> Northrop v. Newtown & Bridgeport Turnpike Co., 3 Conn. 544; Oxford Turnpike Co. v. Bunnel, 6 Conn. 552.

<sup>181</sup> Northrop v. Curtis, 5 Conn. 246; Chambersburg Ins. Co. v. Smith, 11 Pa. St. 120; Cleveland & Mahoning R. Co. v. Robbins, 35 Ohio St. 483; Timberlake v. Shippers' Compress Co., 72 Miss. 323; Hall v. Rose Hill & Evanston Road Co., 70 Ill. 673; Robinson v. New

fer on the books of the corporation, 182 unless he has elected to treat the refusal as a conversion of the stock. 183 But a transferee of shares cannot maintain an action for a dividend until he has applied for a transfer on the books of the corporation in accordance with its by-laws. 184

- —(3) Remedy in equity.—It has been said that a stock-holder may maintain a suit in equity to compel payment of a dividend which has been declared and set apart, 185 but, so long as there is an adequate remedy at law by an action of assumpsit, this is very doubtful. Of course a stockholder is entitled to such relief in equity if there are other grounds for equitable jurisdiction. If the directors declare a dividend payable at such time as they direct, the dividend must be paid within a reasonable time; and if they refuse to pay the same, or to fix any time for payment, stockholders may sue in equity to compel payment. 186
- —(4) Mandamus is not a proper remedy to compel the directors of a corporation to pay a dividend even after it has been declared, 187 although there is dictum in a New York case to the effect that it would lie to compel the delivery of the checks or money to stockholders, where a dividend has not only been de-

Berne Nat. Bank, 95 N. Y. 637, 2 Cum. Cas. 157; Gemmell v. Davis, 75 Md. 546, 32 Am. St. Rep. 412. <sup>182</sup> Robinson v. New Berne Nat. Bank, 95 N. Y. 637, 2 Cum. Cas. 157; Hill v. Atoka Coal & Mining Co. (Mo.) 21 S. W. 508.

Where a corporation has refused to transfer on its books shares of stock transferred by a stockholder to a third party, a purchaser from such third party may maintain an action against the corporation to recover dividends on the stock, without a previous demand or a transfer of the stock to him, and his right of action is not defeated because he cannot compel such transfer in equity. Robinson v. National Bank of New Berne, 95 N. Y. 637, 2 Cum. Cas. 157.

188 Pending an action against a Co., 41 Mich. 166.

corporation for conversion of shares of stock, on its refusal to recognize the plaintiff as a stockholder, he cannot maintain an action for dividends. Hughes v. Vermont Copper Mining Co., 72 N. Y. 207.

184 Sargent v. Essex Marine Ry. Corp., 9 Pick. (Mass.) 202.

185 Le Roy v. Globe Ins. Co., 2 Edw. Ch. (N. Y.) 657, 1 Smith's Cas. 325, 2 Keener's Cas. 1327. See, also, Beers v. Bridgeport Spring Co., 42 Conn. 17, 2 Keener's Cas. 1428; Cook County Brick Oo. v. Kaehler, 83 Ill. App. 448.

<sup>186</sup> Beers v. Bridgeport Spring Co., 42 Conn. 17, 2 Keener's Cas. 1429.

187 People v. Centra Car & Mfg. Co., 41 Mich. 166.

clared, but the money has been set apart in a bank for the payment, and checks drawn for delivery to the stockholders. 188

- —(5) Action against other stockholders.—A person claiming to be a shareholder in a corporation, and entitled to a dividend, but who has not been recognized as such by the corporation in payment of the dividend, cannot maintain an action for money had and received against recognized shareholders for his share. He must enforce his rights by an action against the corporation itself. 189
- —(6) Action against officers of corporation.—Ordinarily a stockholder cannot maintain an action against the treasurer or other officer of the corporation for refusing to pay him a dividend, although there were funds of the corporation in his hands sufficient for the payment of the dividend at the time of such refusal. But it has been held that the treasurer of a corporation, who holds money to pay a dividend which has been declared, and who refuses to pay the dividend on certain shares on the ground that he is himself the owner of the shares, is liable personally in an action of assumpsit for money had and received, brought in the name of the real owner of such shares, to recover the amount of the dividend. 191
- —(7) Set-off of dividend against debt due to corporation.—When a stockholder is sued by the corporation upon a debt due from him to the corporation, he has a right to set off against the claim of the corporation any dividends which have been declared and are due to him.<sup>192</sup> It is otherwise, of course, if no dividend has yet been declared, although there may be surplus profits.<sup>193</sup>

<sup>192</sup> Whittington v. Farmers' Bank of Somerset, 5 Har. & J. (Md.) 489. <sup>193</sup> See ante, § 517(b).

A debtor to a corporation cannot set off, on a judgment thereon against him, the dividend that will be coming to him as a stockholder when its affairs are wound up, even in equity, unless there is an express agreement to set off the debts against each other pro tanto. Ruckersville Bank v. Hemphill, 7 Ga. 396.

 <sup>188</sup> Le Roy v. Globe Ins. Co., 2
 Edw. Ch. (N. Y.) 657, 1 Smith's Cas. 325, 2 Keener's Cas. 1327.

<sup>189</sup> Peckham v. Van Wagenen, 83
N. Y. 40, 38 Am. Rep. 392, affirming
13 Jones & S. (N. Y.) 328.

<sup>&</sup>lt;sup>190</sup> French v. Fuller, 23 Pick. (Mass.) 108. See, also, Smith v. Poor, 40 Me. 415.

<sup>&</sup>lt;sup>191</sup> Williams v. Fullerton, 20 Vt. 346.

- -- (8) Recovery of interest.-When a stockholder demands payment of a dividend, and it is refused, he is entitled to recover interest from the time of such demand and refusal, but he is not entitled to interest before a demand and refusal.194
- (9) Statute of limitations.—Since the relation between a corporation and a stockholder with respect to his share of a dividend which has been declared by the corporation is that of debtor and creditor merely, and not that of trustee and cestui que trust, the statute of limitations runs against an action by a stockholder to recover his share in a dividend which has been declared. 195 even though he may have been credited with his share on the books of the corporation. 196 The action is governed, in the absence of other express statutory provision, by the statute governing actions on implied contract, and the statute begins to run from the time the dividend is payable, 197 provided the stock-

194 State v. Baltimore & Ohio R. 194 State v. Baltimore & Ohio R. Co., 6 Gill (Md.) 363; Bank of Louisville v. Gray, 84 Ky. 565; Keppel v. Petersburg R. Co., Chase, 167, Fed. Cas. No. 7,722; Boardman v. Lake Shore & Michigan Southern Ry. Co., 84 N. Y. 157, 2 Keener's Cas. 1368; Philadelphia, Wilmington & B. R. Co. v. Cowell, 28 Pa. St. 329, 70 Am. Dec. 128; Cochran v. McGee (Ky.) 53 S. W. 519

A stockholder is not entitled to interest on ordinary dividends declared, or on money due him by reason of a reduction of the capital stock, for a period during which the corporation was prevented from paying him the same by attachments of his stock by third persons, although the money was, during such period, mingled with the general assets of the corporation, the corporation being ready and willing to pay over the same but for the attachments. Mustard v. Union Nat. Bank, 86 Me. 177. And see Hagar v. Union Nat. Bank, 63 Me. 509.

The contrary was held in Heck v. Bulkley (Tenn.) 1 S. W. 612, gation in writing for the payment

joined from collecting dividends after they had been declared.

195 In re Severn & Wye & Severn Bridge Ry. Co., 74 Law T. (N. S.) 219, 1 Smith's Cas. 322, 2 Keener's Cas. 1342. Kane v. Bloodgood, 7 Johns. Ch. (N. Y.) 90, 11 Am. Dec. 417; Winchester & Lexington Turnpike Co. v. Wickliffe's Adm'r, 100 Ky. 531, 66 Am. St. Rep. 356; Hunt v. O'Shea, 69 N. H. 600; and cases cited in the notes following.

196 In re Severn & Wye & Severn Bridge Ry. Co., 74 Law T. (N. S.) 219, 1 Smith's Cas. 322, 2 Keener's Cas. 1342.

197 In re Severn & Wye & Severn Bridge Ry. Co., 74 Law T. (N. S.) 219, 1 Smith's Cas. 322, 2 Keener's Cas. 1342; Com. v. Springfield, M. & H. Turnpike Co., 10 Bush (Ky.) 257; Bills v. Silver King Mining Co., 106 Cal. 9.

In a late Kentucky case it was held that, where the declaration of a dividend is a part of the records of the corporation, and is signed by the proper officer, an action to recover a dividend is governed by the limitation of actions upon an obliwhere the corporation had been en- of money. Winchester & Lexingholder has notice of the dividend; 198 and it can make no difference that the corporation had not, at the time of declaring the dividend, given the stockholder a certificate of his shares. 199 When a dividend is payable, not on any specified day, but on demand, the statute, in some jurisdictions, does not begin to run until demand and refusal,200 while in others it begins to run at the time the dividend is declared.201

- (d) Effect of consolidation.—When a corporation which is liable for dividends on its stock is consolidated with another corporation, and the consolidated corporation assumes all its liabilities, it is liable for the dividends.202
- Remedies for unlawful payment of dividends—(a) In general.—The remedies when the directors of a corporation unlawfully pay or threaten to pay dividends are as follows:
- (1) Dividends unlawfully paid may be recovered back by the corporation or its assignee in bankruptcy, or, in equity, by credit-
- (2) A stockholder, or perhaps a creditor, may sue in equity to enjoin unlawful payment of a dividend, or to compel its repayment.
- (3) A bond or note given for an illegal dividend is void except in the hands of a bona fide holder for value.

Adm'r, 100 Ky. 531, 66 Am. St. Rep. 356.

198 St. Romes v. Levee Steam Cotton Press, 20 La. Ann. 381; Philadelphia, Wilmington & B. R. Co. v. Cowell, 28 Pa. St. 329, 70 Am. Dec. 128. Compare Bills v. Silver King Mining Co., 106 Cal. 9.

199 Com. v. Springfield, M. & H. Turnpike Co., 10 Bush (Ky.) 257. See ante, § 378(b).

200 State v. Baltimore & Ohio R. Co., 6 Gill (Md.) 363; Armant v. New Orleans & Carrollton R. Co., 41 La. Ann. 1020; Philadelphia, Wilmington & B. R. Co. v. Cowell, 28 Pa. St. 329, 70 Am. Dec. 128. See, also, Bills v. Silver King Mining Co., 106 Cal. 9; Kobogum v. Jackson Iron Co., 76 Mich. 498:

ton Turnpike Co. v. Wickliffe's Larwill v. Burke, 19 Ohio Cir. Ct. R. 513.

> 201 Winchester & Lexington Turnpike Co. v. Wickliffe's Adm'r, 100 Ky. 531, 66 Am. St. Rep. 356. See, also, Landis v. Saxton, 105 Mo. 486, 24 Am. St. Rep. 403.

> It is otherwise where the corporation is a bank, since it is a part of the business of a bank to receive and hold the money of its patrons payable on demand, and the statute runs only from the time of a demand. Bank of Louisville v. Gray, 84 Ky. 565, as explained in Winchester & Lexington Turnpike Co. v. Wickliffe's Adm'r, 100 Ky. 531, 66 Am. St. Rep. 356.

> 202 Chase v. Vandervilt, 62 N. Y. 307; Boardman v. Lake Shore & Michigan Southern Ry. Co., 84 N. Y. 157, 2 Keener's Cas. 1368. See ante. § 356.

- (4) Directors are liable to the corporation, and, in equity or under statutes, to creditors, for unlawfully paying dividends, if they have acted in bad faith or negligently, but not otherwise.
- (b) Recovery of dividends unlawfully paid—(1) In general.—
  If the directors of a corporation declare and pay a dividend to its stockholders, when there are no profits out of which a dividend may lawfully be declared, the stockholders have no right to retain the money received by them, and it may be recovered from them by the corporation in an action for money had and received, or by an assignee in bankruptcy or receiver of the corporation, or, in equity, by creditors or a receiver, or dissenting stockholders.<sup>203</sup> If a corporation refuses to sue to recover dividends paid out of the capital stock, a stockholder may file a bill to compel repayment.<sup>204</sup>

203 Lexington Life, Fire & Marine Ins. Co. v. Page, 17 B. Mon. (Ky.) 412, 66 Am. Dec. 165; Williams v. Boice, 38 N. J. Eq. 364, 1 Smith's Cas. 339; Gratz v. Redd, 4 B. Mon. (Ky.) 178; Main v. Mills, 6 Biss. 98, Fed. Cas. No. 8,974; Brown v. Finn, 34 Fed. 124; Finn v. Brown, 142 U. S. 56; Curran v. Arkansas, 15 How. (U. S.) 304; Wood v. Dummer, 3 Mason, 308, Fed. Cas. No. 17,944, 1 Cum. Cas. 805, 2 Keener's Cas. 1858; Hayden v. Thompson (C. C. A.) 71 Fed. 60; Bank of St. Marys v. St. John, 25 Ala. 566; Fort Payne Bank v. Alabama Sanitarium, 103 Ala. 358; Hastings v. Drew, 76 N. Y. 9; Bartlett v. Drew, 57 N. Y. 587; Sagory v. Dubois, 3 Sandf. Ch. (N. Y.) 466; Clapp v. Peterson, 104 Ill. 26; Minnesota Thresher Mfg. Co. v. Langdon, 44 Minn. 37; Panhandle Nat. Bank v. Emery, 78 Tex. 498; Reading Trust Co. v. Reading Iron Works, 137 Pa. St. 282; Grant v. Ross, 100 Ky. 44; Grant v. Southern Contract Co. (Ky.) 47 S. W. 1091; In re National Bank of Wales [1899] 2 Ch. 629.

The corporation's right to recover the dividends so paid is not affected by the fact that the payment was made in good faith under a

mistaken belief that sufficient assets would remain to pay debts; nor by the fact that the payment was authorized by the stockholders as a body. Grant v. Ross, 100 Ky. 44.

In some jurisdictions, it was at one time held that an action at law would not lie to recover back dividends unlawfully paid by a corporation out of the capital stock, but that the only remedy was in equity. Vose v. Grant, 15 Mass. 505; Spear v. Grant, 16 Mass. 9; Paschall v. Whitsett, 11 Ala. 472.

That the lawfulness of a dividend is to be determined as of the time when it was declared, see ante, § 520(d).

A corporation which has erroneously or wrongfully paid dividends when there were no profits may assign the right to recover the same from the stockholders to its assignee for the benefit of creditors, Grant v. Ross, 100 Ky. 44.

As to suits by creditors and receivers of the corporation, see post, chapter xxv.

<sup>204</sup> Holmes v. Newcastle-upon-Tyne Freehold Abattoir Co., 1 Ch. Div. 682.

To sustain such a recovery, there need not have been any bad faith or negligence in declaring the dividend.205 Nor need the stockholders have known that the dividend was declared and paid illegally. However innocent their intention may have been. they are not in the position of bona fide holders, for they are bound to know the condition of the corporation, or, rather, they are chargeable with knowledge of its condition.<sup>206</sup>

A director or other officer of a corporation is bound to know the condition of the corporation's affairs, and if he receives a dividend which has not been earned, it may be recovered from him by the corporation or its assignee.207 An officer who receives a dividend which was fraudulently or unlawfully declared is liable to the corporation therefor, although he may have repudiated the transaction after his receipt of the dividend, and repaid it to another officer, for he should repay it to the corporation.208

The fact that a statute makes directors individually liable to the corporation or its creditors for wrongfully paying dividends when there are no profits available for the purpose does not affect the liability of stockholders to repay dividends wrongfully received by them, and, notwithstanding such a statute, the

205 Lexington Life. Fire & Marine Ins. Co. v. Page, 17 B. Mon. (Ky.) 412, 66 Am. Dec. 165.

<sup>206</sup> Lexington Life, Fire & Marine Ins. Co. v. Page, 17 B. Mon. (Ky.) 412, 66 Am. Dec. 165; Finn v. Brown, 142 U. S. 56; Fort Payne Bank v. Alabama Sanitarium, 103 Ala. 358; In re Denham, 25 Ch. Div. 752. Compare In re Peruvian Guano Co. [1894] 3 Ch. 690.

207 Main v. Mills, 6 Biss. 98, Fed. Cas. No. 8,974. And see Gratz v. Redd, 4 B. Mon. (Ky.) 178. See, also, Rance's Case, 6 Ch. App. 104. Compare In re Denham, 25 Ch. Div. 752.

<sup>208</sup> In Finn v. Brown, 142 U. S. 56, affirming Brown v. Finn, 34

was transferred on the books of the bank from the president to the vice president before the latter's election, and after his election a false and fraudulent dividend was declared without his knowledge, and he first learned that the shares had been transferred to him upon being informed that the dividend thereon had been credited to him on the books of the bank. He immediately repudiated the transaction, directed the president to re-transfer the shares to his own name, and then gave the president his check for the amount of the dividend. It was held that he should have repaid the dividend to the bank, and that his payment to the president did not relieve Fed. 124, stock in a national bank him from liability to the bank.

liability of the stockholders may be enforced in equity by a receiver of the corporation.209

- ---(2) Liability of transferee.--A corporation cannot recover from a transferee of shares dividends improperly paid to the transferrer, for the transferee only succeeds to such of the transferrer's liabilities as are incidental to the ownership of the shares.210
- (3) Statute of limitations.—When dividends are unlawfully paid, an action against the stockholders to recover them back is governed by the statute of limitations applicable to actions on implied contract, unless there is some other statute expressly applying to it, and the statute begins to run, in the absence of bad faith on the part of the stockholder, from the time the dividend was paid.<sup>211</sup> But the statute of limitations does not run against a suit in equity by creditors of the corporation, or by a receiver, to recover dividends paid in fraud of the rights of creditors.<sup>212</sup>
- (c) Injunction.—If the directors of a corporation threaten to pay a dividend when there are no profits out of which it may lawfully be paid, any stockholder may maintain a suit in equity on behalf of themselves and other stockholders to enjoin them.<sup>213</sup> It has also been held that such a suit may be maintained by a creditor of the corporation.<sup>214</sup> "Dividends," it was said by Judge Jackson in a late case, "can be rightfully paid only out of profits. Corporations are liable to be enjoined by shareholders or creditors from making a distribution, in dividends,

Eq. 364, 1 Smith's Cas. 339.

210 Hurlbut v. Tayler, 62 Wis.

211 Lexington Life, Fire & Marine Ins. Co. v. Page, 17 B Mon. (Ky.) 412, 66 Am. Dec. 165; Hayden v. Thompson (C. C. A.) 71 Fed.

<sup>212</sup> Williams v. Boice, 38 N. J. Eq. 364, 1 Smith's Cas. 339.

213 Davison v. Gillies, 16 Ch. Div. 347, note, 2 Keener's Cas. 1362, 2 Cum. Cas. 223; Macdougall v. Jersey Imperial Hotel Co., 2 Hem. & M. 528; Coates v. Nottingham Wa-

209 Williams v. Boice, 38 N. J. terworks Co., 30 Beav. 86; Browne v. Monmouthshire Railway & Canal Co., 13 Beav. 32; Bloxam v. Metropolitan Ry. Co., 3 Ch. App. 337; Carpenter v. New York & New Haven R. Co., 5 Abb. Pr. (N. Y.) 277; Coquard v. National Linguist Co., 171, 111. seed Oil Co., 171 Ill. 480.

> As to the sufficiency of a stockholders' bill to enjoin payment of a dividend, see Coquard v. National Linseed Oil Co., 171 Ill. 480, affirming 67 Ill. App. 20.

> 214 Reid v. Eatonton Mfg. Co., 40 Ga. 98, 2 Am. Rep. 563.

of capital."215 A court of equity will not interfere, however, if the declaration or payment of the dividend cannot injure either the stockholders or creditors.216

- (d) Bond or note given for illegal dividend.—If a corporation, instead of paying an unlawful dividend out of capital stock in cash, gives its bonds or notes therefor, they cannot be enforced except by bona fide holders for value, and the stockholders receiving the same do not occupy such a position.217
- (e) Liability of directors.—The directors of a corporation charged with the management of its affairs occupy a relation analogous to that of trustees, and they are certainly liable to the corporation for any breach of trust.218 This principle applies if they unlawfully pay dividends when there are no surplus profits available for their payment, and thereby reduce the capital stock, provided they act in bad faith, or are guilty of gross negligence or inattention. In such a case they incur liability, not only to the corporation, but also, in equity, to creditors. 219 There is no liability, however, either to the corporation or to creditors, if they act in good faith and with due care, unless liability is imposed by some statute. In other words, they are not liable for mere errors of judgment.220

Statutory liability.-In many jurisdictions, statutes have been enacted expressly making the directors or trustees of corporations liable to creditors, as well as the corporation, for paying dividends unlawfully, and thereby diminishing the capital stock. There is no liability under these statutes unless the directors act in bad faith or are guilty of negligence.221

Cas. 1295.

216 Chaffee v. Rutland R. Co., 55

217 Alabama Marble & Stone Co. v. Chattanooga Marble & Stone Co. (Tenn.) 37 S. W. 1004.

218 Post, chapter xxiv. 219 Gratz v. Redd, 4 B. Mon. Co. v. Lacey, 63 N. Y. 422. (Ky.) 178; Scott v. Eagle Fire Co., (Ky.) 178; Scott v. Eagle Fire Co., 221 Excelsior Petroleum Co. v. 7 Paige (N. Y.) 198; Gaffney v. Lacey, 63 N. Y. 422; Rorke v. Colvill, 6 Hill (N. Y.) 567; In re Thomas, 56 N. Y. 559; Van Dyck v.

<sup>215</sup> Mobile & Ohio R. Co. v. Ten-National Funds Assurance Co., 10 nessee, 153 U. S. 486, 2 Keener's Ch. Div. 118. Compare In re National Bank of Wales [1899] 2 Ch. 629. And see post, chapter xxiv., where this question is further

> 220 Lexington & Ohio R. Co. v. Bridges, 7 B. Mon. (Ky.) 556, 46 Am. Dec. 528; Excelsior Petroleum

- § 529. Rights of preferred stockholders—(a) In general.—The right of holders of preferred or guarantied stock to dividends depends, of course, upon the terms of their contract. Ordinarily-
- (1) They are entitled to receive the specified dividend before the payment of any dividend on the common stock.
- (2) Dividends on preferred stock, although guarantied, are payable only out of net earnings or surplus profits available for the purpose of paying dividends, unless there is something to show a contrary intention on the part of the legislature and of the corporation and the stockholders.
- (3) Unless a contrary intention appears, dividends on preferred stock are cumulative, and arrearages in one year are payable in subsequent years, when there are sufficient profits, before dividends can be paid on the common stock.
- (4) Ordinarily it is for the directors to determine whether the condition of the corporation is such that a dividend on preferred stock may be declared; but if they abuse their discretion, a court of equity will compel them to declare a dividend.
- (b) The right to preference.—Ordinary preferred stock, as we have seen, is stock upon which the holders are entitled to certain dividends before payment of any dividends to the holders of the common stock.<sup>222</sup> The extent of the preference depends, of course, upon the terms of the contract under which the stock is issued.\* Preferred stockholders may, by the terms of their contract, be entitled, after payment of the preferred dividend, to

McQuade, 86 N. Y. 38. And see post, chapter xxiv.
222 Ante, § 414 et seq.

the rate of dividend expressed in certificates of preferred stock, where it has not reserved the power to do so either in the certificate of incorporation or the certificate of stock. And the power to do so is not given by a statute authorizing corporations, with the assent of a majority in interest of its stockholders, to amend its certificate of incorporation as of the date of the filing and recording of Distributing Co., 58 N. J. Eq. 97.

Where a corporation agreed to pay a person all dividends on cer-222 Ante, § 414 et seq. tain shares on which he held an \*A corporation cannot reduce option during the period of the terate of dividend expressed in option, and that it would make good any deficiencies in the dividends below four per cent. per annum, but did not guaranty payment of dividends annually or at any stated period, and the dividend paid the first year exceeded four per cent. for the whole period of the option, and no further dividends were declared, it was held that the company's liability was discharged by the payment made. the original. Pronick v. Spirits Fontana v. Pacific Can Co., 129 Cal. 51.

share equally with the common stockholders in any further dividends that may be declared,223 or to share in any surplus after payment of a specified dividend on the common stock.224

(c) Dividends payable out of profits only.—Preferred stockholders, as was explained in a former chapter, are not creditors of the corporation, even though the specified dividends may in terms be "guarantied," so as to be entitled to dividends irrespective of the condition of the corporation and the existence of profits.<sup>225</sup> On the contrary, they are stockholders, and in the same position substantially as the other stockholders, except as to the right to a preference. And it is well settled that they are entitled to dividends only when there are surplus profits or net earnings out of which dividends may lawfully be paid, as in the case of common stockholders.<sup>226</sup> "It is now well established that dividends on preferred stock are payable only out of net earnings which are applicable to the payment of dividends; and that such dividends are not payable absolutely and unconditionally as interest is, but only out of profits made by the company. The preference is limited to profits whenever earned."227

The fact that the dividends are in terms "guarantied" does not change this rule so as to render them payable absolutely and unconditionally.<sup>228</sup> "It is not a debt that is guarantied, but the

<sup>225</sup> Ante, § 417(c). 226 Ante, § 417(c).
226 Birch v. Cropper, 14 App. Cas.
525; Lockhart v. Van Alstyne, 31
Mich. 76, 18 Am. Rep. 156, 2 Keener's Cas. 1354; Taft v. Hartford,
Providence & F. R. Co., 8 R. I. 310,
5 Am. Rep. 575, 1 Smith's Cas. 347; 5 Am. Rep. 575, 1 Smith's Cas. 547; Miller v. Ratterman, 47 Ohio St. 141; Chaffee v. Rutland R. Co., 55 Vt. 110; Warren v. King, 108 U. S. 389; New York, Lake Erie & W. R. Co. v. Nickals, 119 U. S. 296, 2 Keener's Cas. 1399, 2 Cum. Cas. 228; St. John v. Erie Ry. Co., 10

223 Gordon's Ex'rs v. Richmond, Blatchf. 271, Fed. Cas. No. 12,226, Fredericksburg & P. R. Co., 78 Va. 22 Wall. (U. S.) 136, 2 Keener's 501, 2 Keener's Cas. 1384. Cas. 1348; Bates v. Androscoggin 224 Ashbury v. Watson, 30 Ch. Elfast & Moosehead Lake R. Co. Belfast & Moosehead Lake R. Co. v. City of Belfast, 77 Me. 445; Williston v. Michigan Southern & Northern Indiana R. Co., 13 Allen (Mass.) 400; Field v. Lamson & Goodnow Mfg. Co., 162 Mass. 388; Heller v. National Marine Bank, 89 Md. 602, 73 Am. St. Rep. 212.

227 Veazey, J., in Chaffee v. Rutland R. Co., 55 Vt. 110.

228 Taft v. Hartford, Providence & F. R. Co., 8 R. I. 310, 1 Smith's Cas. 347; Chaffee v. Rutland R. Co., 55 Vt. 110; Lockhart v. Van Alstyne, 31 Mich. 76, 18 Am. Rep. v. City of Belfast, 77 Me. 445; Wil-

right to a dividend from the earnings and income of the corporation. The right to a dividend is not a debt. There is no debt until the dividend is declared. The obligation and right to declare it does not arise until there is a fund from which it can properly be made."229

A contract to pay a stockholder dividends out of capital stock, or to pay absolutely and unconditionally, whether there are profits or not, is illegal and void as against creditors and as against the corporation.230

An agreement to pay dividends on preferred stock out of net earnings does not mean the net earnings of the corporation as it is when the preferred stock is issued, and the corporation may incur new obligations after the agreement which will diminish the net earnings applicable to such dividends.<sup>231</sup>

If a corporation wrongfully pays dividends to its ordinary stockholders when there are no surplus profits out of which dividends may lawfully be declared, as where a railroad company pays dividends without setting aside anything to create a reserve fund for the purpose of repairs and renewals, it cannot, in a subsequent year, set apart such a fund, not only for the current year, but also for preceding years, to the prejudice of preferred stockholders whose right to a dividend in each year is dependent upon the profits of the particular year only. As was said in an English case: "The company either have a right to recover back from the ordinary shareholders any sums overpaid or not. If they have a right, they must recover them; if they have no right to recover them, a fortiori they have no right to recover them from the preference shareholders, and, of course,

v. Ratterman, 47 Ohio St. 141; Williston v. Michigan Southern & Northern Indiana R. Co., 13 Allen (Mass.) 400; Field v. Lamson & Goodnow Mfg. Co., 162 Mass. 388.

229 Chaffee v. Rutland R. Co., 55

280 Guinness v. Land Corpora-ren v. King, 108 U. S. 389.

156, 2 Keener's Cas. 1354; Miller tion of Ireland, 22 Ch. Div. 349, 2 Keener's Cas. 1286: Memphis Grain & Package Elevator Co. v. Memphis & Charleston R. Co., 85

Tenn. 703, 4 Am. St. Rep. 798.
231 St. John v. Erie Ry. Co., 22 Wall. (U. S.) 136, 2 Keener's Cas. 1348, affirming 10 Blatchf. 271, Fed. Cas. No. 12,226. See, also, Warstill less right to take away the dividends from the preference shareholders."232

The principles upon which it is to be determined whether there are net earnings or surplus profits for the purpose of paying a dividend are precisely the same in the case of preferred stock as in the case of common stock, and have been considered in former sections.233

The legislature, of course, may authorize a corporation to issue preferred stock as a means of raising money, and to stipulate for the payment of dividends out of gross earnings,—thus putting the preferred stockholders in the position of creditors. this clearly appears to have been the intention, the courts must give it effect.234

(d) Cumulative dividends.—Sometimes the dividends upon preferred stock are in express terms made to depend upon the profits of each particular year, so that the holders of the stock will not be entitled to any dividends in a particular year if there are not enough profits in that year to pay the same, or will be entitled only in so far as there are profits. In such a case, the dividends are not cumulative, and are not to be made up out of the profits, although sufficient, of subsequent years.235

232 Dent v. London Tramways Rep. 330; Elkins v. Camden & At-Co., 16 Ch. Div. 344, 2 Keener's lantic R. Co., 36 N. J. Eq. 233. Cas. 1360, 2 Cum. Cas. 225. Preferred stockholders are not

233 Ante, §§ 519, 520, and cases there cited.

234 Gordon's Ex'rs v. Richmond, Fredericksburg & P. R. Co., 78 Va. 501, 2 Keener's Cas. 1384. See, also, Williams v. Parker, 136 Mass. 204, 2 Keener's Cas. 1381; Cotting v. New York & New England R. Co., 54 Conn. 156. And see ante, § 417(c).

285 See Dent v. London Tramways Co., 16 Ch. Div. 344, 2 Keener's Cas. 1360, 2 Cum. Cas. 225; New York, Lake Erie & W. R. Co. v. Nickals, 119 U. S. 296, 2 Keener's Cas. 1399, 2 Cum. Cas. 228; Hazeltine v. Belfast & Moosehead Lake R. Co., 79 Me. 411, 1 Am. St.

Preferred stockholders are not entitled to cumulative dividends under articles providing that "the be entitled, out of the net profits of each year, to a preference dividend at the rate of £10 per cent. per annum on the amount for the time being paid or deemed to be paid up thereon. After payment of such preferential dividend the holders of ordinary shares shall be entitled to a like dividend at the rate of £10 per cent. per annum. Subject as aforesaid, the preference and ordinary shares shall rank equally for dividend." Staples v. Eastman Photographic Materials Co. [1896] 2 Ch. 303.

Where certificates of preferred stock issued by a railroad company claring dividends on preferred stock, the arrearages of one year cannot be paid out of the earnings of a subsequent year, when the charter or by-laws require the entire net earnings of each year to be paid out in dividends. In such a case, the preferred stock is noncumulative.<sup>236</sup>

If the contract with the preferred stockholders, however, guaranties or entitles them in general terms to a certain annual dividend, not making the dividend payable in each year dependent upon the profits of that year, the dividends are cumulative, and, if the profits in any year are not sufficient to pay the dividend, it must be paid, in addition to subsequent dividends, out of the profits of subsequent years, before any dividends can be paid to the holders of common stock.<sup>237</sup>

(e) Discretion in declaring dividends.—What has been said in a former section as to the discretion of the directors in declaring or refusing to declare dividends <sup>238</sup> applies to preferred stock,

after reorganization provided that the holders of preferred stock then issued, and such additional amounts as might be issued in pursuance of resolutions, etc., were entitled to receive each year from the surplus net profits of the company for the current year such yearly dividends (non-cumulative) as the board of directors might declare, "up to, but not exceeding, four per centum, before any dividends shall be set apart or paid up on the common the reorganization and agreement authorized the issue of "\$40,000,000 four per cent. noncumulative preferred stock per annum before the payment of any dividend on the common stock," it was held that the preferred stock was noncumulative, and entitled to four per cent. dividends, and no more, out of the earnings of the company, before the payment of dividends on common stock; and that the preferred stockholders were not entitled, after payment of such dividend, to share in the distribution of additional profits. Scott v. Baltimore & Ohio R. Co. (Md.) 49 Atl. 327.

<sup>236</sup> Hazeltine v. Belfast & Moosehead Lake R. Co., 79 Me. 411, 1 Am. St. Rep. 330. See, also, Elkins v. Camden & Atlantic R. Co., 36 N. J. Eq. 233; Staples v. Eastman Photographic Materials Co. [1896] 2 Ch. 303.

237 Henry v. Great Northern Ry. Co., 27 Law J. Ch. 1, 3 Jur. (N. S.) 1133; Smith v. Cork & Bandon Ry. Co., 5 Ir. Rep. Eq. 65; Webb v. Earle, L. R. 20 Eq. 556; Corry v. Londonderry & Enniskillen Ry. Co., 29 Beav. 263; Boardman v. Lake Shore & Michigan Southern Ry. Co., 84 N. Y. 157, 2 Keener's Cas. 1368; Jermain v. Lake Shore & Michigan Southern Ry. Co., 91 N. Y. 483, 2 Keener's Cas. 1411; Hazeltine v. Belfast & Moosehead Lake R. Co., 79 Me. 411, 1 Am. St. Rep. 330; Lockhart v. Van Alstyne, 31 Mich. 76, 18 Am. Rep. 156, 2 Keener's Cas. 1354; Cotting v. New York & New England R. Co., 54 Conn. 156; Elkins v. Camdem & Atlantic R. Co., 36 N. J. Eq. 233; West Chester & Philadelphia R. Co. v. Jackson, 77 Pa. St. 321.

238 Ante. § 517(f).

as well as common stock. Even when the dividends for a particular year are made dependent upon the profits of that year, as declared by the board of directors, it is primarily for the board of directors to determine whether the condition of the company in any particular year is such as to warrant the declaration of a dividend, and the courts will not interfere unless an abuse of discretion is shown.<sup>239</sup> If the directors abuse their discretion, however, and refuse to declare a dividend when it is clear that there are surplus profits available for the purpose, they are subject to the control of a court of equity in a suit by the preferred stockholders to compel them to declare and pay a dividend.<sup>240</sup>

The directors are clearly justified in using earnings for the purpose of making necessary repairs, paying debts, laying by for the creation of a reserve fund to repair, or to pay obligations not yet due, etc., and the circumstances may be such as to justify improvements.<sup>241</sup>

- (f) Stock and scrip dividends.—When preferred stockholders are entitled, after payment of the preferred dividend, to share with the common stockholders in any further dividend, they are entitled to share in a stock or scrip dividend declared out of surplus profits used in improvements, or retained by the corporation.<sup>242</sup>
- (g) Rights of transferees.—In the absence of an agreement to the contrary, a transfer of preferred stock, like a transfer of common stock, whether absolute or as a pledge, carries with it the right to all dividends declared after the transfer, but not

<sup>239</sup> New York, Lake Erie & W. R. Co. v. Nickals, 119 U. S. 296, 2 Keener's Cas. 1399, 2 Cum. Cas. 228, reversing 15 Fed. 575; Field v. Lamson & Goodnow Mfg. Co., 162 Mass. 388; Belfast & Moosehead Lake R. Co. v. City of Belfast, 77 Me. 445; McLean v. Pittsburgh Plate Glass Co., 159 Pa. St. 112; ante, § 517(f).

<sup>240</sup> Hazeltine v. Belfast & Moosehead Lake R. Co., 79 Me. 411, 1 Am. St. Rep. 330; Storrow v. Texas Consolidated Compress Mfg. Ass'n (C. C. A.) 87 Fed. 612. And see ante, § 517(f).

<sup>241</sup> New York, Lake Erie & W. R. Co. v. Nickals, 119 U. S. 296, 2 Keener's Cas. 1399, 2 Cum. Cas. 228, reversing 15 Fed. 575; McLean v. Pittsburgh Plate Glass Co. Lean v. Et 112; Field v. Lamson & Goodnow Mfg. Co., 162 Mass. 388. See ante, § 520.

242 Gordon's Ex'rs v. Richmond,

dividends declared before the transfer.243 And it carries, in the absence of agreement to the contrary, the right to receive arrears of dividends when a dividend shall be declared.244

- (h) Remedies of preferred stockholders.—As in the case of common stockholders, preferred stockholders have no legal right to any part of the profits of the corporation until a dividend has been declared, and before then they cannot maintain an action at law against the corporation.245 Nor can they resort to  $mandamus.^{246}$ They may maintain an action at law against the corporation after a dividend has been declared.<sup>247</sup> And they may maintain a suit in equity for relief if the corporation attempts to pay a dividend to the common stockholders before payment of the stipulated dividend on the preferred stock, or to compel the directors to declare and pay a dividend on the preferred stock where they abuse their discretion in refusing to do And if a dividend has been declared, and has been paid to the common stockholders in violation of the rights of preferred stockholders, the latter may maintain assumpsit.249
  - II. RIGHT TO INSPECT BOOKS AND PAPERS OF THE CORPORATION.
- § 530. In general.—At common law, a stockholder has a right to inspect and make abstracts or copies from the books and papers of the corporation, personally or by an agent, if the request to be allowed to do so is made at a reasonable time, and for a specific and

Fredericksburg & P. R. Co., 78 Va. 501, 2 Keener's Cas. 1384.

501, Z Keener's Cas. 1384.

248 Boardman v. Lake Shore & Michigan Southern Ry. Co., 84 N.

Y. 157, Z Keener's Cas. 1368; Jermain v. Lake Shore & Michigan Southern Ry. Co., 91 N. Y. 483, Z Keener's Cas. 1411; Manning v. Quicksilver Mining Co., 24 Hun (N. Y.) 360; Bates v. Androscoggin & Kennebec R. Co. 49 Me. 491 & Kennebec R. Co., 49 Me. 491. And see ante, § 525(c).

244 See the cases in the note pre-

245 Williston v. Michigan Southern & Northern Indiana R. Co., 13 Allen (Mass.) 400; ante, § 517(b).

246 Ante, § 527(c)(4).

247 Ante, § 527(c)(1).

248 Smith v. Cork & Bandon Ry. Co., 5 Ir. Rep. Eq. 65; Boardman v. Lake Shore & Michigan Southern Ry. Co., 84 N. Y. 157, 2 Keener's Cas. 1368; Thompson v. New York & Erie R. Co., 45 N. Y. 468; Hazel-tine v. Belfast & Moosehead Lake R. Co., 79 Me. 411, 1 Am. St. Rep. 330; Gordon's Ex'rs v. Richmond, Fredericksburg & P. R. Co., 81 Va. 621. And see ante, §§ 517(f), 527(c)(3).

<sup>249</sup> West Chester & Philadelphia R. Co. v. Jackson, 77 Pa. St. 321; Coey v. Belfast & Co. Down Ry. Co., 2 Ir. C. L. 112.

proper purpose. And he may enforce this right by mandamus, or perhaps in equity by injunction, or maintain an action for damages against the officer denying him the right, or, in a proper case, against the corporation.

In many states, this right is regulated by express statutory provisions.

It is a well-established general rule of the common law, sometimes expressly declared with some modification or change <sup>250</sup> by statute or by the constitution, or by provisions in charters, articles of association, or by-laws, that every stockholder of a private corporation has a right, by reason of his interest therein, to inspect and examine its books and papers, if he asserts the right at reasonable times, and for proper purposes; and he cannot lawfully be denied this right by the officers of the corporation or the other stockholders.<sup>251</sup> "There can be no question

<sup>250</sup> See post, § 531.

251 England: Reg. v. Mariquita & New Granada Mining Co., 1 El. & El. 289; Rex v. Merchant Tailors' Co., 2 Barn. & Adol. 115; Foster v. Bank of England, 8 Q. B. 689; Rex v. Clear, 4 Barn. & C. 899; Nelson v. Anglo-American Land Mortgage Agency Co. [1897] 1 Ch. 130.

United States: Ranger v. Champion Cotton-Press Co., 51 Fed. 61; Chable v. Nicaragua Canal Construction Co., 59 Fed. 846.

Alabama: Foster v. White, 86 Ala. 467; Winter v. Baldwin, 89 Ala. 483.

Delaware: Swift v. State, 7 Houst. 338, 40 Am. St. Rep. 127. Florida: Alabama & Florida

R. Co. v. Rowley, 9 Fla. 508.

Illinois: Stone v. Kellogg, 62-Ill. App. 444, 165 Ill. 192, 56 Am. St. Rep. 240; Meysenburg v. People, 88 Ill. App. 328.

Iowa: Ellsworth v. Dorwart, 95 Iowa, 108, 58 Am. St. Rep. 427.

Louisiana: Hatch v. City Bank of New Orleans, 1 Rob. 470; Legendre v. New Orleans Brewing Ass'n, 45 La. Ann. 669, 40 Am. St. Rep. 243; State v. Bienville Oil Works Co., 28 La. Ann. 204; Cockburn v. Union Bank of Louisiana, 13 La. Ann. 289; State v. New Orleans Gaslight Co., 49 La. Ann. 1556; State v. Citizens' Bank of Jennings, 51 La. Ann. 426.

Michigan: People v. Walker, 9 Mich. 328.

Missouri: State v. St. Louis & San Francisco Ry. Co., 29 Mo. App. 301; State v. Sportsman's Park & Club Ass'n, 29 Mo. App. 326; State v. Laughlin, 52 Mo. App. 542.

New Jersey: Huylar v. Cragin Cattle Co., 40 N. J. Eq. 392; Mitchell v. Rubber Reclaiming Co. (N. J. Eq.) 24 Atl. 407.

New York: People v. Throop, 12 Wend. 183; People v. Mott, 1 How. Pr. 247; People v. Eadie, 63 Hun, 320, 133 N. Y. 573; In re Steinway, 31 App. Div. 70.

Ohio: Cincinnati Volksblatt Co. v. Hoffmeister, 62 Ohio St. 189, 78 Am. St. Rep. 707.

Pennsylvania: Com. v. Phoenix Iron Co., 105 Pa. St. 111, 51 Am. Rep. 184. 1 Smith's Cas. 248; Phoenix Iron Co. v. Com., 113 Pa. St. 563.

Rhode Island: Lyon v. American Screw Co., 16 R. I. 472.

Vermont: Lewis v. Brainerd, 53 Vt. 519.

that the ownership of stock confers the authority to see that the property is well managed. The exercise of this authority involves primarily the right to examine the books."252 holder also has the right to make abstracts, memoranda, and copies. "The right to make copies, and to make abstracts and memoranda, of documents, books and papers, by a stockholder in an incorporated company, is as full and complete as the right of inspection thereof."253

Some of the courts have held that stockholders have a right to inspect the books and papers of the corporation without first showing any mismanagement, where they wish to make the examination in good faith for the purpose of seeing whether its affairs are properly managed. "Such a right," said the New Jersey court, "is necessary to their protection. To say that they have the right, but that it can be enforced only when they have ascertained, in some way without the books, that their affairs have been mismanaged, or that their interests are in danger, is practically to deny the right in the majority of cases. Oftentimes frauds are discoverable only by examination of the books by an expert accountant."254 This, however, is not the doctrine at common law, as established by the decisions, and laid down in the text books. By the weight of authority, in the absence of a statute making the right of examination absolute. there must be something more than bare suspicion of mismanagement or fraud. There must be at least specific and reasonable grounds for suspicion. The right of a stockholder to examine the books and papers of the corporation is not unlimited.

thal, 72 Wis. 314.

The fact that the corporation is in the hands of a receiver does not necessarily deprive stockholders of this right. People v. Cataract Bank, 5 Misc. Rep. (N. Y.) 14. Compare Chable v. Nicaragua Canal Construction Co., 59 Fed. 846.

Wisconsin: State v. Bergen- Brewing Ass'n, 45 La. Ann. 669, 40 Am. St. Rep. 243.

253 Swift v. State, 7 Houst. (Del.) 338, 40 Am. St. Rep. 127. See, also, Cincinnati Volksblatt Co. v. Hoffmeister, 62 Ohio St. 189, 78 Am. St. Rep. 707; Nelson v. Anglo-American Land Mortgage Agency Co. [1897] 1 Ch. 130. And see post, § 261, note.

254 Huylar v. Cragin Cattle Co., 252 Legendre v. New Orleans 40 N. J. Eq. 392.

as is the right of a partner to examine the books and papers of the partnership. He can insist upon and enforce the right when he has a good and specific reason for making the examination, and where his purpose is a proper one, but not otherwise. cannot do so from mere curiosity, or for merely speculative purposes, or for reasons not connected with his rights as a stockholder, or vexatiously, but, at common law at least, he can do so only when he asserts the right "in good faith, and for a specific, honest purpose, and where there is a particular matter in dispute involving and affecting seriously his rights as a stockholder."255

A stockholder cannot make use of his relation as such to inspect the books of the corporation, where his purpose is merely to obtain information for use as a debtor of the corporation.<sup>256</sup> Nor can a stockholder compel a corporation to allow him to examine its books or papers, where his purpose is hostile to the interests of the corporation, and in the interest of a rival corporation, in which he is also a stockholder or otherwise interested.<sup>257</sup> A stockholder, however, cannot be denied the right to inspect the books and papers of the corporation on the ground

St. 237; Lyon v. American Screw Co., 16 R. I. 472; Rex v. Merchant Tailors' Co., 2 Barn. & Adol. 115; Ellsworth v. Dorwart, 95 Iowa, 108, 58 Am. St. Rep. 427; Heminway v. Heminway, 58 Conn. 443; People v. Walker, 9 Mich. 328; People v. Lake Shore & Michigan Sauther. Lake Shore & Michigan Southern Lake Shore & Michigan Southern R. Co., 11 Hun (N. Y.) 1; Sage v. Lake Shore & Michigan Southern Ry. Co., 70 N. Y. 220; People v. Northern Pacific R. Co., 18 Jones & S. (N. Y.) 456; State v. Einstein, 46 N. J. Law, 479.

"There is no express rule that to warrant an application to inspect corporation documents there must actually have been a suit instituted; but it is necessary that there phia v. Eldridge, 2 Pa. Dist. R. 394. actually have been a suit institutshould be some particular matter

255 Phoenix Iron Co. v. Com., 113 in dispute, between members, or Pa. St. 563; Com. v. Phoenix Iron between the corporation and indi-Co., 105 Pa. St. 111, 51 Am. Rep. viduals in it; there must be some 184, 1 Smith's Cas. 248; Com. v. controversy, some specific purpose Empire Passenger Ry. Co., 134 Pa. in respect of which the examinain respect of which the examina-tion becomes necessary." Rex v. Merchant Tailors' Co., 2 Barn. & Adol. 115.

> On petition for a writ of mandamus by the holders of four shares of a large corporation, to allow them to inspect the stock ledger of the company, it was held that, to show a right to the writ, they must show some controversy pending, or some question at issue, as to which the contents of the book were of consequence, and that it was not enough to show an ex-pectation of benefit from knowing the contents. Lyon v. American Screw Co., 16 R. I. 472.

257 Heminway v. Heminway, 58

of hostility to the management or officers, where he has a good reason for making the examination.258

To be entitled to inspect the books and papers of a corporation, one must be a stockholder at the time he seeks to exercise the right.\*

## § 531. Express provisions in the charter, general law, articles of association, or by-laws.

In some jurisdictions, the right of stockholders to inspect and examine the books and papers of the corporation is not left to be determined by the common law, but is regulated by statute or by the constitution, and sometimes the right is given in express terms by the charter or articles of association of a corporation, or regulated by its by-laws. And when the right is so given or regulated, it is sometimes more absolute than it is at common law, according to the cases referred to in the preceding section.

Under a general statute, as a statute providing that the stockholders of all private corporations shall "have the right of access to, inspection and examination of the books, records and papers of the corporation, at reasonable and proper times," it is to be implied that the inspection and examination shall not be from mere idle curiosity, or for speculative purposes, or for purposes hostile to the interests of the corporation, and by the express provisions of the statute the right must be asserted at "reasonable and proper times;" but these are the only limita-

40 N. J. Eq. 392; Ellsworth v. Dorwart, 95 Iowa, 108, 58 Am. St. Rep. ple, 88 Ill. App. 328.

person, to be by him delivered & Wheless, 104 La. 125.

Compare, however, when the parties should fully com-Meysenburg v. People, 88 Ill. App. ply with their obligations, and afterwards, while the stock and 258 Huylar v. Cragin Cattle Co., notes were thus held in escrow, the sellers made a demand on the corporation to be permitted to inspect 427. And see Meysenburg v. Peo- its books, and, on its refusal, applied for a writ of mandamus, it Where stockholders sold their was held that the transaction was stock under an agreement which not a mere agreement to sell, but provided that the certificates and a completed sale, passing the title the notes given in payment should to the stock, and the writ was be placed in the hands of a third therefore denied. State v. Whited tions upon the right. It is not necessary to show any particular reason or occasion for making the inspection and examination.<sup>259</sup> In an Alabama case, involving a construction of a statute in the language above quoted, it was said: "The statute was enacted in view of the restrictions and limitations placed by the common law upon the exercise of the right; and the purpose is to protect small and minority stockholders against the power of the majority, and against the mismanagement and faithlessness of agents and officers, by furnishing mode and opportunity to ascertain, establish and maintain their rights, and to intelligently perform their corporate duties. \* \* \* The only express limitation is, that the right shall be exercised at reasonable and proper times; the implied limitation is, that it shall not be exercised from idle curiosity, or for improper or unlawful purposes. In all other respects, the statutory right is absolute. The shareholder is not required to show any reason or occasion rendering an examination opportune and proper, or a definite or legitimate purpose. The custodian of the books and papers cannot question or inquire into his motives and purposes. If he has reason to believe that they are improper or illegitimate, and refuses the inspection on this ground, he assumes the burden to prove them such. If it be said, this construction of the statute places it in the power of a single shareholder to greatly injure and impede the business, the answer is, the legislature regarded his interests in the successful promotion of the objects of the corporation a sufficient protection against unnecessary or injurious interference. The statute is founded on the principle, that the shareholders have a right to be fully informed as to the condition of the corporation, the manner in which its affairs are

259 Foster v. White, 86 Ala. 467; Co., 50 Barb. (N. Y.) 280; People Winter v. Baldwin, 89 Ala. 483; v. Paton, 5 N. Y. St. Rep. 313; Ellsstone v. Kellogg, 165 Ill. 192, 56 worth v. Dorwart, 95 Iowa, 108, 58 Am. St. Rep. 240; Cincinnati Am. St. Rep. 427; State v. St. Volksblatt Co. v. Hoffmeister, 62 Louis & San Francisco Ry. Co., 29 Ohio St. 189, 78 Am. St. Rep. 707; Mo. App. 301; State v. Sportsman's State v. Bergenthal, 72 Wis. 314; Park & Club Ass'n, 29 Mo. App. Cotheal v. Brouwer, 5 N. Y. Leg. 326; State v. Laughlin, 53 Mo. Obs. 175, 10 Barb. 216, 5 N. Y. 562; App. 542. People v. Pacific Mail Steamship

conducted, and how the capital, to which they have contributed, is employed and managed."260

A statute giving a stockholder the right to inspect and examine books and papers of the corporation gives him the right to make abstracts, memoranda, or copies thereof.261

Where a statute or by-law gives stockholders a right to examine books and papers of a corporation to a specified extent or at specified times only, they can only claim, under the statute or by-law, such rights as it expressly confers.<sup>262</sup> A statute, however, giving stockholders an absolute right to inspect certain books or papers, or to inspect them at a particular time, but containing no negative words, does not deprive a stockholder of his common-law right to inspect other books or papers, or to inspect them at other reasonable times.<sup>263</sup> And of course, by-laws

Rep. 240.

On petition of a stockholder for a writ of mandamus to enforce his statutory right to inspect the books of a corporation, it was held that an answer setting forth that the animosity torelator cherished wards the company's president, and had threatened to injure the business of the company by disclosing its business secrets to customers and business rivals, showed no ground for denying the writ. Meysenburg v. People, 88 Ill. App. 328.

 <sup>261</sup> Cotheal v. Brouwer, 5 N. Y.
 Leg. Obs. 175, 10 Barb. 216, 5 N. Y. 562; Martin v. W. J. Johnston Co., 62 Hun (N. Y.) 557, 17 N. Y. Supp. 133; Nelson v. Anglo-American Land Mortgage Agency Co. (1897) 1 Ch. 130. And see note

253. supra.

Contra, Com. v. Empire Passen-

ger Ry. Co., 134 Pa. St. 237.

262 See People v. Pacific Mail Steamship Co., 50 Barb. (N. Y.) 280; State v. Bergenthal, 72 Wis. 314; Lyon v. American Screw Co., 16 R. I. 472.

It has been held that a by-law of a corporation, providing that the

260 Foster v. White, 86 Ala. 467. treasurer shall keep full books of And see, to the same effect, Stone account of the business of the corv. Kellogg, 165 Ill. 192, 56 Am. St. poration, "which books shall at all times be open to the inspection of any of the stockholders," does not apply to the stock ledger. Lyon v. American Screw Co., 16 R. I. 472.

The power conferred by the general corporation act of New Jersey (P. L. 1896, p. 292, § 44) to summarily order books of a corporation to be brought within the state "on proper cause shown," can be exercised only when the judicial authority whose action is invoked can exercise control over the books after compliance with the order. Fuller v. Alex. Hollander & Co. (N. J.) 47 Atl. 646.

Where a statute requires a corporation to keep books showing certain matters for inspection of stockholders, a stockholder cannot be deprived of the right to inspect them because they are kept in a particular way, or because they contain, besides the information to which he is entitled, other information, which he has no right to demand. People v. Pacific Mail Steamship Co., 50 Barb. (N. Y.)

263 People v. Lake Shore & Mich-

of a corporation to which a stockholder does not consent cannot deprive him of his common-law right.

A general statute giving stockholders in "all private corporations" the right to inspect and examine the books and papers of the corporation applies to national banks to the same extent as other corporations, at least in the absence of conflicting legislation by congress.264

The liability to the penalty prescribed by such statutes is considered in another section. 265

## Examination by attorney or agent.

When a stockholder has sufficient reason for making an examination of the books or papers of the corporation, he need not necessarily do so in person, but may do so through his attorney, or an expert accountant, or other agent. 266

## § 533. Remedies of stockholders on denial of right.

Mandamus.—If the officers of a corporation wrongfully deny a stockholder the right to inspect its books or papers, he may enforce his right by writ of mandamus, unless this remedy is excluded by statute.<sup>267</sup> The writ may issue against the corpora-

igan Southern Ry. Co., 11 Hun (N. Y.) 1; Sage v. Lake Shore & Michigan Southern Ry. Co., 70 N. Y. 220; People v. Eadie, 63 Hun (N. Y.) 320, 133 N. Y. 573.

264 Winter v. Baldwin, 89 Ala.

265 See post, § 533.

266 Foster v. White, 86 Ala. 467; Cincinnati Volksblatt Co. v. Hoffmeister, 62 Ohio St. 189, 78 Am. St. Rep. 707; State v. Bienville Oil Works Co., 28 La. Ann. 204; Ellsworth v. Dorwart, 95 Iowa, 108, 58 Am. St. Rep. 427; Mitchell v. Rubber Reclaiming Co. (N. J. Eq.) 24 Atl. 407; People v. Nassau Ferry Co., 86 Hun (N. Y.) 128.

Compare People v. United States Mercantile Reporting Co., 20 Abb. N. C. (N. Y.) 192.

Throop, 12 Wend. (N. Y.) 183; In Throop, 12 wend. (N. Y.) 183; in re Steinway, 31 App. Div. (N. Y.) 70, 159 N. Y. 250; People v. Eadie, 63 Hun, 320, 133 N. Y. 573; Swift v. State, 7 Houst. (Del.) 338, 40 Am. St. Rep. 127; Stone v. Kellogg, 62 Ill. App. 444, 165 Ill. 192, 56 Am. St. Rep. 240; Com. v. Phoenix Iron Co., 105 Pa. St. 111, 51 Am. Rep. 184, 1 Smith's Cas. 248; Phoenix Iron Co. v. Com., 113 Pa. St. 563; State v. Bienville Oil Works Co., 28 La. Ann. 204; Cockburn v. Union Bank, 13 La. Ann. 289; Legendre v. New Orleans Brewing Ass'n, 45 La. Ann. 669, 40 Am. St. Rep. 243; State v. New Orleans Gaslight Co., 49 La. Ann. 1556; State v. Bergenthal, 72 Wis. 314; Lyon v. American Screw Co., 16 R. 20 Abb. N. C. (N. Y.) 192.

1. 472; People v. Walker, 9 Mich.

287 Rex v. Merchant Tailors' Co., 328; Foster v. White, 86 Ala. 467;

2 Barn & Adol. 115; People v. Winter v. Baldwin, 89 Ala. 483;

tion, or against both the corporation and the officer having the custody of the books or papers.268 Or it may issue against the officer alone, without making the corporation a party.<sup>269</sup> statute gives a stockholder a particular remedy within the corporation, he must resort to that remedy before he can resort to mandamus.270

A writ of mandamus may issue to enforce the right of a nonresident stockholder to inspect and take copies of documents of a foreign corporation, if they are in the custody of an agent within the state.<sup>271</sup> And the court may compel a domestic corporation to bring its books and papers into the state for an inspection, where they are kept in another state.272

In Ohio, and it may be in other states, the statutes are such that mandamus will not lie as at common law. In Ohio, where the statute declares that the writ of mandamus "must not be issued in a case where there is a plain and adequate remedy in the ordinary course of the law," it has been held that mandamus will not lie to compel a corporation or its officers to allow an in-

Huylar v. Cragin Cattle Co., 40 N. J. Eq. 392; Fuller v. Alex. Hollander & Co. (N. J.) 47 Atl. 646; Trimble v. American Sugar-Refining Co. (N. J. Ch.) 48 Atl. 912; Meysenburg v. People, 88 Ill. App. 328; Nelson v. Anglo-American Land Mortgage Agency Co. [1897] 1 Ch. 130.

To be entitled to the writ, the relator must be a stockholder at the time it is to be issued. It will not be issued if he has sold his stock. State v. Whited & Wheless, 104 La. 125.

268 Reg. v. Mariquita & New Granada Mining Co., 1 El. & El. 289; Rex v. Merchant Tailors' Co., 2 Barn. & Adol. 115; Com. v. Phoenix Iron Co., 105 Pa. St. 111, 51 Am. Rep. 184, 1 Smith's Cas. 248; Phoenix Iron Co. v. Com., 113 Pa. St. 563; Cockburn v. Union Bank, 13 La. Ann. 289; Lyon v. American Screw Co., 16 R. I. 472; Huylar v. Compare Huylar v. Cragin Cattle Co., 40 N. J. Eq. 392. tle Co., 42 N. J. Eq. 139.

269 People v. Throop, 12 Wend. (N. Y.) 183; Swift v. State, 7 Houst. (Del.) 338, 40 Am. St. Rep. 127; Stone v. Kellogg, 62 Ill. App. 444, 165 Ill. 192, 56 Am. St. Rep. 240; Foster v. White, 86 Ala. 467; State v. Represental 72 Wis 215. State v. Bergenthal, 72 Wis. 314.

In Louisiana, however, it has been held that, in mandamus proceedings to enforce the right to inspect the books of a corporation, the citation should be addressed to the corporation, and not to its manager. State v. North American Land & Timber Co., 105 La. 379.

<sup>270</sup> People v. Nassau Ferry Co., 86 Hun (N. Y.) 128.

<sup>271</sup> Swift v. State, 7 Houst. (Del.) 338, 40 Am. St. Rep. 127.

272 Huylar v. Cragin Cattle Co., 40 N. J. Eq. 392; Mitchell v. Rubber Reclaiming Co. (N. J. Eq.) 24 Atl. 407.

Compare Huylar v. Cragin Cat-

spection of its books and papers, as there is an adequate remedy by injunction.273

In equity.—Stockholders have generally enforced their right to inspect the books and papers of the corporation by mandamus. and there are very few reported cases in which it has been sought to enforce the right in equity by injunction. It has been held, however, in some jurisdictions, that a suit for an injunction will lie.274 Of course, a court of equity has jurisdiction to enforce the right of inspection, if the circumstances are such that mandamus will not afford an adequate remedy, or if there are other grounds of equitable jurisdiction.\*

Recovery of damages.—If an officer of a corporation, having the custody of its books and papers, wrongfully refuses to allow a stockholder to inspect the same, he is guilty of a wrong against the stockholder, and is liable in an action for damages.<sup>275</sup>

The corporation itself will undoubtedly be liable in damages for denial of a stockholder's right to inspect books and papers, if it can be regarded as in default in the matter, as where the

<sup>273</sup> Cincinnati Volksblatt Co. v. Hoffmeister, 62 Ohio St. 189, 78 Am. St. Rep. 707.

274 Cincinnati Volksblatt Co. v. Hoffmeister, 62 Ohio St. 189, 78 Am. St. Rep. 707; Ranger v. Champion Cotton-Press Co., Fed. 61; Nelson v. Anglo-American Land Mortgage Agency Co. [1897] 1 Ch. 130. But see Fuller v. Alex. Hollander & Co. (N. J.) 47

\* Huylar v. Cragin Cattle Co., 40 N. J. Eq. 392; Ranger v. Champion Cotton-Press Co., 51 Fed. 61.

While a court of equity may, in its discretion, order the officers of a corporation to allow a stockholder to inspect its books at any stage of the proceedings, it will not do so upon the mere filing of the bill, necessity," since the defendants may deny that the complainant is may deny that the complainant is a shareholder, or may set up that Brewing Ass'n, 45 La. Ann. 669, 40 the charter or by-laws modify his Am. St. Rep. 243.

right to such inspection. Ranger v. Champion Cotton-Press Co., 51 Fed. 61.

A bill in equity by a stockholder, asking the aid of the court to enforce the right to inspect the books of the corporation, must show that there has been a denial of the right, or it will be demurrable. Coquard v. National Linseed Oil Co., 171 Ill. 480.

In New Jersey it is held that, where a stockholder wishes a discovery of the financial condition of the company, his remedy is not by a bill in equity for a discovery, but by mandamus to enforce the right to inspect its books, aided, if necessary, by a petition under the statute to compel the corporation to bring the books into the state for or after service and before answer, such purpose. Trimble v. Amer-"except under the most pressing ican Sugar-Refining Co. (N. J. Ch.) 48 Atl. 912.

inspection is refused by or by order of the board of directors or the majority stockholders as a body. It has been held, however, that a stockholder cannot hold his co-stockholders or the corporation liable in damages on account of the refusal by a subordinate officer of an informal request to be allowed to inspect books or papers of the corporation, although he would have ascertained that the affairs of the corporation were being improperly managed, and might have taken steps to avoid loss. refusal, he should apply for a writ of mandamus, or else apply to the directors, so as to put the company in default. damus had issued immediately after the refusal," said the Louisiana court in such a case, "the action would have been maintained against the company only. It would have had the right to repudiate the refusal and permit the inspection. The act of the secretary is not absolutely binding upon the company in matter of inspection of the books. He cannot stand in judgment, nor can he as agent of the stockholders occasion damages by refusing the books, for which the company will be liable to one stockholder to the loss of the others, who are not parties and have not given the least sanction to the refusal. error of an officer in a subordinate position in refusing to permit books to be examined is not per se such an error as will expose the company to the payment of damages."276

Statutory penalty.—When the right of a stockholder to inspect the books and papers of the corporation is regulated by statute, a specific penalty is sometimes imposed upon the corporation, or upon the officer denying him the right, to be recovered in an action by the stockholder or by the state. And the penalty may be recovered without showing any actual pecuniary damage. All that is necessary is to show a wrongful denial of the right.<sup>277</sup>

276 Legendre v. New Orleans Brewing Ass'n, 45 La. Ann. 669, 40 Am. St. Rep. 243. See Fuller v. Alex. Hollander & Co. (N. J.) 47 Atl. 646.

<sup>277</sup> Kelsey v. Pfaudler Process Fermentation Co., 51 Hun (N. Y.) 636.

Under the New York stock corporation law (section 29) providing that every such corporation shall keep at its office a stock book containing the names of all stockholders, etc., which shall be open daily for inspection by its stockholders, and that for negligence or

When the corporation or an officer has wrongfully denied to a stockholder the right to examine its books, his right to sue for the statutory penalty is fixed, and is not affected by the fact that he was allowed to make the examination upon a subsequent application.278

Where a statute imposes upon the custodian of the books and papers of a corporation the duty to allow stockholders to inspect the same, the duty is an incident of his office, and he cannot be relieved therefrom by a by-law of the corporation, or by any resolution or orders of the directors, so long as he continues in office, and has the legal custody of the books and papers.<sup>279</sup> officer is not liable to the penalty if the books and papers have been taken from his custody by the directors, so that it is not within his power to allow an inspection, provided, at least, he has not participated in putting them beyond his control for the very purpose of shirking his duty, and defeating a stockholder's right of inspection,<sup>280</sup> and provided he states the reason why he cannot allow an inspection.<sup>281</sup> If the books and papers come back into his custody after he has refused a request to be allowed to inspect them, it is his duty to notify the stockholder, and give him an opportunity to inspect them.<sup>282</sup>

Reasonable or unavoidable delay in allowing an inspection, as because the books are locked up in the safe, and the only officer who knows the combination is absent, does not subject the cor-

refusal to allow such inspection president, a short distance away, the corporation shall forfeit to the people fifty dollars for every day of such neglect or refusal, and that every officer or agent of the corporation who shall willfully neglect or refuse to exhibit such books shall be liable to the same penalty, the penalty is not incurred, either by the corporation or by its officers or agents, in the absence of such neglect or refusal. Where a stock-holder, therefore, on three occasions, called at the general office of a corporation, and was informed by its agent that the stock books were at the office of the company's

and that he could inspect them by calling there, and on one occasion he went there and took copies from the books, it was held that neither the company nor the agent was liable under the statute. Lozier v. Saratoga Gas, Electric Light & Power Co., 59 App. Div. (N. Y.)

278 Kelsey v. Pfaudler Process Fermentation Co., 51 Hun (N. Y.)

279 Lewis v. Brainerd, 53 Vt. 519.

280 Id. 281 Id.

282 Id.

poration or its officers to a penalty,-but such an excuse cannot be made in bad faith, and for the purpose of defeating the stockholder's right.283

III. CONTRACTS AND CONVEYANCES BETWEEN A CORPORATION AND ITS STOCKHOLDERS.

In general.—In the absence of fraud, a contract or conveyance between a corporation and a stockholder is as valid as a contract or conveyance between a corporation and a stranger.

Since a corporation is a legal entity distinct from its members,284 there is nothing to prevent a stockholder from entering into a contract with the corporation, or taking a conveyance of property from it, or executing a conveyance to it. A contract or conveyance between a corporation and one or more of its stockholders is just as valid as a contract or conveyance between a corporation and a stranger, 285 if the stockholder is not also acting as the agent of the corporation in the transaction.<sup>286</sup> stockholder, therefore, may lend money to the corporation, and take a mortgage to secure the loan, and, in the absence of fraud, he has the same rights under such a contract as a stranger would have.287 A stockholder guarantying the notes of the corporation may receive collateral security from the corporation to in-

Fire & Marine Ins. Co. v. Page, 17 B. Mon. (Ky.) 412, 66 Am. Dec. 165; International Wrecking & Transportation Co. v. McMorran, 73 Mich. 467; Sawyer v. Royalton Methodist Episcopal Soc., 18 Vt. 405; Rogers v. Danby Universalist
Soc. 19 Vt. 187; Foster v. Commissioners of Inland Revenue
[1894] 1 Q. B. Div. 516, 1 Smith's chett v. Blair (C. C. A.) 100 Fed.
Cas. 40, 1 Keener's Cas. 41; Rogers v. Nashville, Chattanooga & St. L. 268; post, chapter xxiv.

 <sup>283</sup> Kelsey v. Pfaudler Process Ry. Co. (C. C. A.) 91 Fed. 299;
 Fermentation Co., 41 Hun (N. Y.) Ryan v. Williams, 100 Fed. 172;
 20, 51 Hun (N. Y.) 636, 3 N. Y. Hanchett v. Blair (C. C. A.) 100 20, 51 Hun (N. Y.) 636, 3 N. Y. Hanchett V. Blair (C. C. A.) 100 Fed. 817; Gamble v. Queens County Water Co., 123 N. Y. 91; Kane 285 Pope v. Brandon, 2 Stew. v. Lodor, 56 N. J. Eq. 268; Rich-(Ala.) 401, 20 Am. Dec. 49; Gor ardson v. Graham, 45 W. Va. 134; don v. Preston, 1 Watts (Pa.) 385, Langston v. Greenville Land & 26 Am. Dec. 75; Lexington Life. Improvement Co., 120 N. C. 132; Wills v. Porter (C. C. A.) 100 Wills v. Porter (Cal.) 61 Pac. 1109; Kingman & Co. v. Cornell-Tebbetts Machine & Buggy Co., 150 Mo. 282; Wolf v. Pennsylvania R. Co., 195 Pa. St. 91. And see post, chapter xxiv.

demnify him.<sup>288</sup> Where a corporation is allowed to prefer creditors on making an assignment for the benefit of creditors. it may prefer a stockholder who is a creditor.<sup>289</sup>

While a stockholder may contract with the corporation, such a contract cannot be made the means of defrauding creditors of the corporation. The relation of a stockholder to the corporation, and to the public who deal with the corporation, are such as to require good faith and fair dealing in every transaction between him and the corporation which may injuriously affect the rights of creditors or of the general public, and a rigid scrutiny will be made into all such transactions in the interest of creditors; and if there is any fraud or unfair dealing to the prejudice of creditors, they will be entitled to relief.290

Nor can a stockholder of a corporation take advantage of his position, or of the influence which he may have by reason thereof, to perpetrate a fraud upon other stockholders in his dealings with the corporation.\*

- IV. ACTIONS BY STOCKHOLDERS TO ENFORCE INDIVIDUAL RIGHTS, OR RE-DRESS OR PREVENT INDIVIDUAL INJURIES.
- In general.—A stockholder or member of a corporation has the same right as a stranger to sue the corporation or its officers or agents to enforce his individual rights, or obtain redress for individual injuries.

When an injury is to stockholders individually, and not to the corporation, the corporation cannot sue.

Since a corporation is a legal entity distinct from its members, the rule that a person cannot sue himself does not apply to an action between a corporation and its members. It is well settled, therefore, that a member or stockholder of a corporation may sue the corporation either at law or in equity.<sup>291</sup>

<sup>&</sup>lt;sup>288</sup> Kingman & Co. v. Cornell- S.) 610, 2 Smith's Cas. 812, 2 Keen-Tebbetts Machine & Buggy Co., er's Cas. 1873. See post, chapter

<sup>150</sup> Mo. 282; post, chapter xxiv.

289 Lexington Life, Fire & Marine Ins. Co. v. Page, 17 B. Mon.

Co., 184 Pa. St. 102. And see post, (Ky.) 412. See post, chapter xxv. chapter xxiv., where many cases 290 Sawyer v. Hoag, 17 Wall. (U. are collected.

course a stockholder may sue the officers or agents of the corporation to enjoin or redress any injury to himself in his individual capacity.

Thus, a stockholder may sue the corporation to recover a dividend after it has been declared, for he then has a right to the money in his individual capacity.292 A stockholder or member of a corporation may also proceed against a corporation, or its officers in a proper case, by an action at law for damages, or by a suit in equity, or by mandamus, according to the circumstances. where he is wrongfully refused a certificate of stock;293 where he is wrongfully expelled and denied the rights of membership;294 where his shares are wrongfully forfeited or sold for nonpayment of assessments;295 where the corporation or its officers wrongfully refuse to recognize a valid transfer of stock;296 where they recognize an unauthorized or forged transfer and issue a certificate, thereby depriving him of his stock;<sup>297</sup> where they wrongfully refuse to allow him to inspect the books and papers of the corporation, 298 or to vote at corporate meetings; 299 where he was induced to purchase his stock by fraud for which the corporation or its officers are responsible;300 where there is a fraudulent and unequal disposition of unissued stock in violation of his right to a proportionate share;301 or where he is wrongfully denied the right to subscribe for or purchase a proportionate share of increased stock; 302 and in many other cases.

291 Waring v. Catawba Co., 2 Bay (S. C.) 109, 1 Smith's Cas. 39; Henderson v. San Antonio & Mexican Gulf R. Co., 17 Tex. 560, 67 Am. Dec. 675; Culbertson v. Waham. Dec. 0/3; Cultertson V. Wabash Navigation Co., 4 McLean, 544, Fed. Cas. No. 3,464; Samuel v. Holladay, Woolw. 400, Fed. Cas. No. 12,288; Peirce v. Partridge, 3 Metc. (Mass.) 44; Gray v. Portland Bank, 3 Mass. 364, 3 Am. Dec. 156; Barnstead v. Empire Mining Co., 5 Cal. 299; Wilson v. First Nat. Bank of Cheyenne, 1 Wyo. 108; Cary v. Schoharie Valley Machine Co., 2 Hun (N. Y.) 110; Leonard v. Spencer, 108 N. Y. 338; Sawyer v. Royalton Methodist

Episcopal Soc., 18 Vt. 405; Rogers v. Danby Universalist Soc., 19 Vt. 187; Wausau Boom Co. v. Plumer, 35 Wis. 274.

292 Ante, § 527(c).

<sup>293</sup> Ante, § 378. 294 Ante, § 373 (d).

<sup>295</sup> Ante, § 495.

<sup>296</sup> Post, § 593 et seq.

297 Post, § 602 et seq.

298 Ante, § 533. 299 Post, chapter xxiv.

300 Ante, § 472.

301 Reese v. Bank of Montgomery County, 31 Pa. St. 78, 72 Am. Dec. 726; ante, § 388.

802 Gray v. Portland Bank, 3

A stockholder may sue the corporation to abate a nuisance maintained by it, where he has not co-operated in or encouraged its erection;303 or to recover damages for the maintenance of a nuisance.304

Individual rights of stockholders and injuries against stockholders individually cannot be enforced or redressed in an action by the corporation, but the action must be by the stockholders individually. Thus, a corporation cannot maintain a suit in equity to enjoin the collection of an illegal tax upon the shares of its stock in the hands of individual stockholders, except when the corporation is required by statute to pay the tax.305

- V. REMEDIES OF STOCKHOLDERS FOR INJURIES TO THE CORPORATION.
- In general.—A stockholder cannot, under any circumstances, unless by statute, maintain an action at law against the corporation, or its officers or agents, or third persons, to enforce a right belonging to the stockholders collectively, or to redress an injury to the stockholders collectively, but the action must be brought by the corporation.

As a general rule, the same is true of suits in equity to enforce rights belonging to the corporation, or to enjoin or redress injuries to the corporation. A stockholder may sue in equity, however, in order to protect his equitable rights, if he cannot obtain relief through the corporation. He may sue in equity on his own behalf, or on behalf of himself and the other stockholders who may come in:

- (1) When there is some action or threatened action of the board of directors or trustees which is beyond the powers conferred upon the corporation by its charter or other source of organization.
- (2) Or where there is such a fraudulent transaction completed or contemplated by the board of directors or trustees in connection with some third person or corporation, or among themselves, or

Mass. 364, 3 Am. Dec. 156; ante, §

303 Leonard v. Spencer, 108 N. Kenna, 32 Minn. 468. See ante, § Y. 538.

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304 Burbank v. West Walker River Ditch Co., 13 Nev. 431. 305 Waseca County Bank v. Mc-

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with other stockholders, as will result in serious injury to the corporation, or to the interests of the other shareholders.

- (3) Or where the board of directors or trustees, or a majority of them, are acting for their own interest, in a manner destructive of the corporation itself, or of the rights of the other shareholders.
- (4) Or where the majority of the shareholders are oppressively and illegally pursuing a course, in the name of the corporation, which is in violation of the rights of the other shareholders, and which can only be restrained by the aid of a court of equity.
- (5) But before the stockholder can maintain a suit in his own name, where the right of action is in the corporation, he must show to the satisfaction of the court that he has exhausted all the means within his reach to obtain relief or redress within the corporation itself. He must have made an earnest effort to induce remedial action on the part of the board of directors or trustees, and, failing with them, to obtain action by the stockholders as a body, if there was time to do so, or he must show that the circumstances were such that such an effort would have been useless.
- (6) A stockholder cannot sue where the act complained of, or the refusal of the directors to sue, is properly within their discretionary powers, or, generally, the discretionary powers of a majority of the stockholders.
- (7) A stockholder cannot sue in such cases where he has been guilty of laches, or is estopped by participation, consent, or acquiescence.

In the preceding sections, we have considered the rights of a stockholder or member of a corporation to maintain actions at law and suits in equity against the corporation and its officers or agents to enforce rights which belong to him individually, or to prevent or redress injuries to him individually. We are now to deal with the remedies of stockholders to enforce rights belonging to all the stockholders collectively,—or to the corporation, as distinguished from the individual stockholders,—and to enjoin or redress injuries to the corporation. This distinction between the individual and the collective rights of stockholders is of the greatest importance.

As was shown in a former chapter, a corporation, unlike a mere partnership, is an artificial person or legal entity distinct

from its stockholders.<sup>306</sup> As a distinct legal entity, it takes and holds the title to its property, manages its business through its agents, makes its contracts, and conveys its property. If it makes a contract, the rights accruing under the contract are the rights of the corporation, and not the rights of the stockholders individually. Even when all the stock of a corporation is owned by one person, the rights under a contract by the corporation are its rights, and not the rights of the individual. Except as hereafter explained, such rights, therefore, must be enforced, not by the stockholders individually, but by the corporation.<sup>307</sup>

In like manner, if the property of a corporation is converted by a stranger, or if a trespass is committed thereon, or if an injury to its property is caused by the negligence of another, or if an injury is threatened, the injury is to the corporation, not to the stockholders individually, and it is for the corporation, and not for the stockholders as individuals, to take proper steps, by action or otherwise, to prevent or redress the injury.<sup>308</sup>

This is true when a corporation is injured by the fraud, excess of authority, or negligence of its officers or agents. The injury is primarily to the corporation, and not to the individual stockholders, and it is for the corporation to seek redress.<sup>309</sup>

### § 537. Actions at law to redress injuries to the corporation.

Since the rights arising out of the contracts of a corporation belong to it, and not to the stockholders individually, and injuries to the property of the corporation caused by the wrongful acts or negligence of others are injuries to the corporation itself, it necessarily follows that any action at law to enforce such a contract, or recover damages for its breach, or to obtain redress for such injuries, must be brought by the corporation in the corporate name, and through its managing officers. Neither a single stockholder nor all the stockholders, as individuals, can maintain an action at law in their own names upon a contract made by the corporation, or for injuries committed against

<sup>808</sup> Ante, §§ 5, 6. 807 Post, §§ 537, 538, 543.

<sup>&</sup>lt;sup>808</sup> Post, §§ 537, 543. <sup>809</sup> Post, §§ 537, 543.

the property of the corporation as trespass, trover for the conversion of property, an action on the case for injuries caused by the acts or negligence of another, or an action of replevin or ejectment to recover corporate property. All such actions must be brought in the corporate name, and cannot be maintained by stockholders in their own names, either on their own behalf because of their equitable interest in the property of the corporation, or on behalf of the corporation. This principle applies. whether the wrongs complained of are the acts or negligence of strangers, or the fraudulent or wrongful acts or negligence of the directors or managing officers of the corporation.<sup>310</sup> fact that one person owns all the stock of a corporation does not enable him to sue in his own name for an injury to the corporation, for the corporation is none the less a separate and distinct person in the law.311

As stated above, it makes no difference in the application of this rule that the injury is caused by the officers of the corporation in their management of its affairs. Misfeasance or negligence on the part of the managing officers of a corporation, resulting in loss of its assets, is an injury to the corporation, for which it must sue. A stockholder cannot sue for damages because his stock is rendered worthless.312 A stockholder has no

310 Button v. Hoffman, 61 Wis. rine Ry. Co., 18 Me. 35; Smith v. 20, 50 Am. Rep. 131, 1 Smith's Cas. Poor, 40 Me. 415; Kennebec & 33, 1 Keener's Cas. 33, 1 Cum. Cas. Portland R. Co. v. Portland & Ken-38; Smith v. Hurd, 12 Metc. (Mass.) 371, 46 Am. Dec. 690, 1 Smith's Cas. 253, 2 Keener's Cas. Thompson v. Stanley, 20 N. Y. 1526, 1 Cum. Cas. 792; Tomlinson v. Bricklayers Union, No. 1, 87 Ind. v. Bricklayers Union, No. 1, 87 Ind. tral & Hudson River R. Co., 35 308, 1 Cum. Cas. 33; Cutshaw v. Fargo, 8 Ind. App. 691; Bartlett v. Dudley, 111 Mich, 437.

Brickett, 14 Allen (Mass.) 62; Bennett v. American Art Union. 5 20. 50 Am Ren. 131 1 Smith's Cas. nett v. American Art Union, 5 Sandf. (N. Y.) 614; Talbot v. Scripps, 31 Mich. 268; People v. State Treasurer, 24 Mich. 468; Allen v. Curtis, 26 Conn. 456; Gorham v. Gilson, 28 Cal. 479; McAfee v. Zettler, 103 Ga. 579; Steele Lum-ber Co. v. Laurens Lumber Co., 98 Ga. 329; Bethune v. Wells, 94 Ga. Mich. 437. 486; Hodsdon v. Copeland, 16 Me. 312 Smith v. Hurd, 12 Metc. 314; Drinkwater v. Portland Ma- (Mass.) 371, 46 Am. Dec. 690, 1

Portland R. Co. v. Portland & Kennebec R. Co., 54 Me. 173; Faurie v. Millaudon, 3 Mart. (N. S.; La.) 476; Thompson v. Stanley, 20 N. Y. Supp. 317; Niles v. New York Central & Hudson River R. Co., 35 Misc. Rep. (N. Y.) 69; Randall v. Dudley, 111 Mich. 437.

311 Button v. Hoffman, 61 Wis. 20, 50 Am. Rep. 131, 1 Smith's Cas. 33, 1 Keener's Cas. 33, 1 Cum. Cas. 38. where it was held that the

38, where it was held that the owner of all the stock of a corporation could not maintain an action of replevin to recover property belonging to the corporation.

See, also, Randall v. Dudley, 111 Mich. 437.

right of action against the corporation because of a depreciation in the value of his stock in common with the rest of the stock, but must show some injury and damage peculiar to himself.313

At law there no exception to this rule, even when the corporation refuses to sue. In such a case, however, as we shall see in the following sections, the stockholders have their remedy in equity.

If a stockholder or other person has in his hands money accruing from a sale of corporate property, another stockholder cannot recover any part of it in an action for money had and received, without the consent of the corporation, for it belongs to the corporation, and not to the stockholders individually. But if the corporation has directed or consented that the money shall be distributed among the stockholders, it then belongs to the stockholders individually, and any stockholder may maintain such an action to recover his proportion.314

#### The general right of stockholders to sue in equity.

Under ordinary circumstances, when redress or preventive relief is sought for a wrong committed or threatened against a corporation, whether by strangers or by its officers, or where it is sought to enforce contracts or other rights of a corporation, the same principle applies to suits in equity as to actions at law. Except as hereafter shown, the suit must be brought by the corporation itself in the corporate name, and cannot be brought by a stockholder on his own behalf, or on behalf of himself and others.315 In equity, however, the rule is not inflexible, as it is at law. In a proper case, a court of equity will look beyond the

Smith's Cas. 253, 2 Keener's Cas. River R. Co., 35 Misc. Rep. (N. Y.) 1526, 1 Cum. Cas. 792; Niles v. New York Central & Hudson River R. Co., 35 Misc. Rep. (N. Y.) 69; and other cases cited in note 310, supra.

A stockholder cannot sue to recover damages for foreclosure of a mortgage in fraud of minority 461, 1 Smith's Cas. 267, 2 Keener's stockholders, for the right of access. 1588, 1 Cum. Cas. 693; Russell tion is in the corporation. Niles v. Wakefield Waterworks Co. L. v. New York Central & Hudson R. 20 Eq. 474, 1 Smith's Cas. 291, 1

313 Oliphant v. Woodburn Coal & Mining Co., 63 Iowa, 332.

314 Hodsdon v. Copeland, 16 Me. 314; Drinkwater v. Portland Marine Ry. Co., 18 Me. 35.

corporate body as a legal entity distinct from its members,316 and, disregarding the fiction, will recognize the fact that a corporation is in reality an association of individuals for the purpose of private gain, like an ordinary partnership, 317 and that, while they have not the legal title to the assets of the corporation, they are nevertheless the beneficial or equitable owners. And if an injury is committed or threatened against the corporation which will constitute a violation of the equitable rights of stockholders, and for any reason a dissenting stockholder cannot obtain redress or relief through the corporation, a court of equity will grant appropriate relief in a suit brought by him in his own behalf, or in behalf of himself and other stockholders who may come in and be made parties, according to the circumstances. Such a suit is generally brought and sustained because the corporation is in the control of the persons who have committed or threatened to commit the wrongs complained of.318

221; Smith v. Poor, 40 Me. 415, 63 Am. Dec. 672; Hersey v. Veazie, 24 Me. 9, 41 Am. Dec. 364; Booth v. Robinson, 55 Md. 419; Dunphy v. Traveller Newspaper Ass'n, 146 Mass. 495, 1 Cum. Cas. 769; Cates v. Sparkman & Wise County Coal Co., 73 Tex. 619, 15 Am. St. Rep. 806; Hazard v. Durant, 11 R. I. 195; Rathbone v. Parkersburg Gas Co., 31 W. Va. 798; Slattery v. St. Louis & New Orleans Transp. Co., 91 Mo. 217, 60 Am. Rep. 245; Wallace v. Lincoln Savings Bank, 89 Tenn. 630, 24 Am. St. Rep. 625; Cunningham v. Wechselberg, 105 Wis. 359; and many other cases hereafter cited. See infra, section 543.

316 Ante, §§ 5, 6. 317 Ante. § 7.

318 England: Foss v. Harbottle, 2 Hare, 461, 1 Smith's Cas. 267, 2

Cum. Cas. 725; Macdougall v. Keener's Cas. 1588, 1 Cum. Cas. Gardiner, 1 Ch. Div. 13, 2 Keener's 693; Atwool v. Merryweather, L. Cas. 1632, 1 Cum. Cas. 704; Hawes v. Oakland, 104 U. S. 450, 1 273, 1 Cum. Cas. 717; Menier v. Smith's Cas. 282, 2 Keener's Cas. Hooper's Telegraph Works, 9 Ch. 1647, 1 Cum. Cas. 756; Brown v. App. 350, 1 Smith's Cas. 287, 1 Vandyke, 8 N. J. Eq. 795, 55 Am. Cum. Cas. 722; Russell v. Wakebee. 250; Bacon v. Irvine, 70 Cal. 1616 Materworks Co., L. R. 20 Eq. 221. Smith v. Poor. 40 Me. 415, 63, 474, 1 Smith's Cas. 291, 1 Cum. field Waterworks Co., L. R. 20 Eq. 474, 1 Smith's Cas. 291, 1 Cum. Cas. 725; Mason v. Harris, 11 Ch. Div. 97, 2 Keener's Cas. 1639, 1 Cum. Cas. 731; Simpson v. Westminster Palace Hotel Co., 8 H. L. Cas. 712, 6 Jur. (N. S.) 985.

United States: Dodge v. Woolsey, 18 How. 331, 2 Keener's Cas. 1605, 1 Smith's Cas. 257, 1 Cum. Cas. 739; Chicago City Ry. Co. v. Allerton, 18 Wall. 233, 1 Keener's Cas. 867, 1 Cum. Cas. 752; Davenport v. Dows, 18 Wall. 626, 1 Smith's Cas. 280, 2 Keener's Cas. 1631, 1 Cum. Cas. 754; Zabriskie v. Cleveland, Columbus, & C. R. Co., 23 How. 381; Hawes v. Oakland. 104 U. S. 450, 1 Smith's Cas. 282, 2 Keener's Cas. 1647, 1 Cum. Cas. 756; Hardon v. Newton, 14 Blatchf. 376, Fed. Cas. No. 6,054, 1 Cum. Cas. 487.

Alabama: Nathan v. Tompkins,

A controversy between the members of a corporation is not within a statute giving equity jurisdiction in controversies between partners, joint tenants, and tenants in common, for stockholders do not stand in either of these relations.<sup>319</sup>

# § 539. Suits to enjoin or set aside ultra vires transactions, and prevent diversion or misapplication of assets.

While a corporation, for the purpose of holding and managing its property, and carrying on its business, is in law an entity or artificial person distinct from the stockholders who compose it, the stockholders are the real parties in interest. Each stockholder has contributed his share of the capital stock under a contract with the corporation, by which the corporation has agreed to hold and manage the same for the purpose of carrying out the objects for which it was created, and for no other purpose, and

82 Ala. 437; Parsons v. Joseph, 92 Ala. 403, 1 Smith's Cas. 311, 2 Keener's Cas. 1653.

California: Cogswell v. Bull, 39 Cal. 320; Burbank v. Dennis, 101 Cal. 90.

Connecticut: Pratt v. Pratt, Read & Co., 33 Conn. 446, 2 Keener's Cas. 1421, 2 Cum. Cas. 219; Allen v. Curtis, 26 Conn. 456.

Illinois: Harding v. American Glucose Co., 182 Ill. 551, 74 Am. St. Rep. 189.

Indiana: Wayne Pike Co. v. Hammons, 129 Ind. 368.

Kansas: Burnes v. City o

Atchison, 48 Kan. 517. Louisiana: In re Belton, 47 La. Ann. 1614.

Maryland: Booth v. Robinson, 55 Md. 419.

Massachusetts: Peabody v. Flint, 6 Allen, 52, 1 Smith's Cas. 263, 1 Cum. Cas. 795; Brewer v. Boston Theatre, 104 Mass. 378.

Michigan: Miner v. Belle Isle Ice Co., 93 Mich. 97, 2 Cum. Cas.

Minnesota: Rothwell v. Robinson, 39 Minn. 1, 12 Am. St. Rep.

Missouri: Exter v. Sawyer, 146 Mo. 302.

New Hampshire: March v. Eastern R. Co., 40 N. H. 548, 77 Am. Dec. 732.

New York: Robinson v. Smith, 3 Paige (N. Y.) 222, 24 Am. Dec. 212; Greaves v. Gouge, 69 N. Y. 154; Brinckerhoff v. Bostwick, 88 N. Y. 52.

Rhode Island: Hodges v. New England Screw Co., 1 R. I. 312, 53 Am. Dec. 624; Hazard v. Durant, 11 R. I. 195.

Tennessee: Black v. Huggins, 2 Tenn. Ch. 780; Wallace v. Lincoln Savings Bank, 89 Tenn. 630, 24 Am. St. Rep. 625.

Texas: Mussina v. Goldthwaite, 34 Tex. 125, 7 Am. Rep. 281; Cates v. Sparkman & Wise County Coal Co., 73 Tex. 619, 15 Am. St. Rep. 806.

Vermont: Stevens v. Rutland & Burlington R. Co., 29 Vt. 545. Wisconsin: Eschweiler v. Stowell, 78 Wis. 316, 23 Am. St. Rep.

411.
And see many other cases more specifically cited under the sections following.

319 Pratt v. Bacon, 10 Pick. (Mass.) 123; Russell v. McLellan, 14 Pick. (Mass.) 63.

every stockholder has a right to insist that this contract shall be complied with. In equity, therefore, a trust is created by implication in favor of the stockholders, that the corporation will not so manage its business or affairs as to defeat the objects for which it was created, and that it will use and apply its assets for the purpose of carrying out those objects, and not divert them to other purposes.320 Nothing, therefore, is now more surely settled in the law of corporations than the doctrine that any unauthorized act or contract by the directors or a majority of the stockholders of a corporation, which will destroy the existence of the corporation, or render it unable to perform its functions, or any misapplication or diversion of assets to purposes not authorized by its charter, even though all other stockholders may consent, is a breach of trust towards a dissenting stockholder, against which he is entitled to relief in equity. Any stockholder, therefore, may maintain a bill in equity in his own name, if he is not estopped,321 and if he cannot obtain relief through the corporation or its officers, 322 to enjoin a misapplication or diversion of its assets, or to enjoin or set aside ultra vires acts or contracts which will result in such a misapplication or diversion, or which may destroy the corporation, or render it unable to carry out its objects. 323 In a leading English case it was said on

320 "As the shareholders are in substance partners in a trading concern the management of which is committed to the body corporate, a trust is by implication created in favor of the shareholders that the corporation will manage the corporate affairs, and apply the corporate funds for the purpose of carrying out the original speculation." Taylor v. Chichester & Midhurst Ry. Co., L. R. 2 Exch. 378. See, also, Russell v. Wakefield Water Works Co., L. R. 2 Makefield Water Works Co., 2 Russ. Water Works Co., 2 Russ. Water Works Co., 2 Russ. 2 Makefield Water Works Co., L. R. 2 Makefield Water Works Co., L. R. 2 Makefield Water Works Co., 2 Russ. Water Works Co., 2 Russ. 2 Makefield Water Works Co., 2 Russ. the corporate funds for the pur-

<sup>321</sup> Post, § 553.

<sup>322</sup> Post. § 543.

<sup>323</sup> England: Tomkinson Southeastern Ry. Co., 35 Ch. Div. 675, 1 Smith's Cas. 300; Seaton v. Grant, 2 Ch. App. 459, 1 Smith's Cas. 307; Colman v. Eastern Counties Ry. Co., 10 Beav. 1, 1 Keener's Cas. 446, 1 Cum. Cas. 136; Cunliff

this point: "It is a breach of trust towards a shareholder in a joint-stock incorporated company, established for certain definite purposes prescribed by its charter, if the funds or credit of the company are, without his consent, diverted from such purposes, though the misapplication be sanctioned by the votes of a majority, and, therefore, he may file a bill in equity against the

Blatchf. 376, Fed. Cas. No. 6,054, 1 Cum. Cas. 487; Davenport v. Dows, 18 Wall. 626, 1 Smith's Cas. 280, 2 Keener's Cas. 1631, 1 Cum. Cas. 754; Bronson v. La Crosse & Milwaukee R. Co., 2 Wall. 283, 1 Smith's Cas. 278; Hawes v. Oakland, 104 U. S. 450, 1 Smith's Cas. 282, 2 Keener's Cas. 1647, 1 Cum. Cas. 756; Greenwood v. Union Freight R. Co., 105 U. S. 13, 2 Smith's Cas. 720, 1 Keener's Cas. 192, 1 Cum. Cas. 538; Zabriskie v. Cleveland, Columbus & C. R. Co., 23 How. 381; Easun v. Buckeye Brewing Co., 51 Fed. 156; Forbes v. Memphis, El Paso & P. R. Co., 2 Woods, 323, Fed. Cas. No. 4,926; Pond v. Vermont Valley R. Co., 12 Blatchf. 280, Fed. Cas. No. 11,265; Eldred v. American Palace Car Co., 96 Fed. 59; Metcalf v. American School-Furniture Co., 108 Fed. 909.

Alabama: Bliss v. Anderson, 31 Ala. 612, 70 Am. Dec. 511; Nathan v. Tompkins, 82 Ala. 437; Memphis & Charleston R. Co. v. Woods, 88 Ala. 630, 16 Am. St. Rep. 81; Parsons v. Joseph, 92 Ala. 403, 1 Smith's Cas. 311, 2 Keener's Cas. 1653; Perry v. Tuskaloosa Cotton Seed Oil Mill Co., 93 Ala. 364; Elyton Land Co. v. Dowdell, 113 Ala. 177, 59 Am. St. Rep. 105; Decatur Mineral Land Co. v. Palm, 113 Ala. 531, 59 Am. St. Rep. 140; Morris v. Elyton Land Co., 125 Ala. 263; Jasper Land Co. v. Wallis, 123 Ala. 652.

Arizona: Henshaw v. Salt River Valley Canal Co. (Ariz.) 54 Pac. 577.

Arkansas: Ex parte Booker, 18 Ark. 338; Mississippi, Ouachita & R. R. R. Co. v. Cross, 20 Ark. 443.

Colorado: People's Savings Bank v.Colorado Mining Exchange Building Co., 8 Colo. App. 354. Connecticut: Sears v. Hotchkiss, 25 Conn. 171, 65 Am. Dec. 557; Scofield v. Eighth School District, 27 Conn. 499; Pratt v. Pratt, Read & Co., 33 Conn. 446, 2 Keener's Cas. 1421, 2 Cum. Cas. 219; Byrne v. Schuyler Electric Mfg. Co., 65 Conn. 336.

Georgia: Central R. Co. v. Collins, 40 Ga. 582, 1 Keener's Cas. 706; Hazlehurst v. Savannah, Griffin & N. A. R. Co., 43 Ga. 13; Cherokee Iron Co. v. Jones, 52 Ga.

276.

Illinois: Bradley v. Ballard, 55 Ill. 413, 8 Am. Rep. 656; City of Chicago v. Cameron, 22 Ill. App. 91, 120 Ill. 447; Kadish v. Garden City Equitable Loan & Building Ass'n, 151 Ill. 531, 42 Am. St. Rep. 256; Harding v. American Glucose Co., 182 Ill. 551, 74 Am. St. Rep. 189; Green v. Hedenberg, 159 Ill. 489, 50 Am. St. Rep. 178; Bruschke v. Nord Chicago Schuetzen Verein, 145 Ill. 433; Stebbins v. Perry County, 167 Ill. 567.

Indiana: McCray v. Junction R. Co., 9 Ind. 358; Tippecanoe County v. Lafayette, Muncie & B. R. Co., 50 Ind. 85; Rogers v. Lafayette Agricultural Works, 52 Ind. 297.

Iowa: Teachout v. Des Moines Broad-Gauge Street Ry. Co., 75 Iowa, 722; Carson v. Iowa City Gaslight Co., 80 Iowa, 638.

Maryland: Davis v. Gemmell,

73 Md. 530.

Massachusetts: Peabody v.Flint, 6 Allen, 52, 1 Smith's Cas. 263, 1 Cum. Cas. 795; Blair v. Telegram Newspaper Co., 172 Mass. 201.

Minnesota: Stewart v. Erie & Western Transp. Co., 17 Minn. 372; Small v. Minneapolis Electro-Matrix Co., 45 Minn. 264; Pencille v. State Farmers' Mutual Hail Ins. Co., 74 Minn. 67, 73 Am. St. Rep.

company in his own behalf to restrain the company by injunction from any such diversion or misapplication."324 And in a leading case in the supreme court of the United States it was said: "It is now no longer doubted, either in England or the United States, that courts of equity, in both, have a jurisdiction over corporations, at the instance of one or more of their members; to apply preventive remedies by injunction, to restrain those who administer them from doing acts which would amount to a violation of charters, or to prevent any misapplication of their capitals or profits, which might result in lessening the dividends of stockholders, or the value of their shares, as either may be protected by the franchises of a corporation, if the acts intended to be done create what is in the law denominated a breach of trust. And the jurisdiction extends to inquire into, and to enjoin, as the case may require that to be done, any proceedings

Missouri: Exter v. Sawyer, 146 Mo. 302.

Montana: Forrester v. Boston & Montana Consolidated Copper & Silver Mining Co., 21 Mont. 544.

Fitzgerald v. Fitz-Nebraska: gerald & Mallory Construction Co., 41 Neb. 374.

New Hampshire: March v. Eastern R. Co., 40 N. H. 548, 77 Am. Dec. 732; Id., 43 N. H. 515; Pearson v. Concord R. Corp., 62 N. H. 537, 13 Am. St. Rep. 590.

New Jersey: Gifford v. New Jersey R. & Transp. Co., 10 N. J. Eq. 171; Zabriskie v. Hackensack & New York R. Co., 18 N. J. Eq. 178, 90 Am. Dec. 617, 2 Smith's Cas. 760, 2 Keener's Cas. 1487, 1 Cum. Cas. 781; Kean v. Johnson, 9 N. J. Eq. 401, 1 Keener's Cas. 608; Elkins v. Camden & Atlantic R. Co., 36 N. J. Eq. 5.

New York: Abbot v. American Hard Rubber Co., 33 Barb. (N. Y.) 578; Leslie v. Lorillard, 110 N. Y. 519, 1 Keener's Cas. 465; Flynn v. Brooklyn City R. Co., 9 App. Div. 324 Cunliff v. Manchester & Bol-269, 158 N. Y. 493; Davis v. Conton Canal Co., 2 Russ. & M. 481.

326; Morrill v. Little Falls Mfg. gregation Beth Tephila Israel, 40 Co., 46 Minn. 260. App. Div. (N. Y.) 424.

North Carolina: Greenville & Raleigh Plank Road Co., 3 Jones' Eq. 183.

Ohio: Taylor v. Miami Exporting Co., 5 Ohio, 162, 22 Am. Dec.

Pennsylvania: Langolf v. Seiberlitch, 2 Pars. Eq. Cas. 64; Manderson v. Commercial Bank, 28 Pa. St. 379.

Rhode Island: rant, 11 R. I. 195. Hazard v. Du-

South Carolina: Stahn v. Catawba Mills, 53 S. C. 519.

Tennessee: Wallace v. Lincoln Savings Bank, 89 Tenn. 630, 24 Am. St. Rep. 625.

Texas: Cates v. Sparkman & Wise County Coal Co., 73 Tex. 619, 15 Am. St. Rep. 806.

Stevens v. Rutland Vermont: & Burlington R. Co., 29 Vt. 545, 1 Smith's Cas. 233.

Virginia: Baltimore & Ohio R. Co. v. City of Wheeling, 13 Grat.

West Virginia: Boyce v. Montauk Gas Coal Co., 37 W. Va. 73.

by individuals, in whatever character they may profess to act. if the subject of complaint is an imputed violation of a corporate franchise, or the denial of a right growing out of it, for which there is not an adequate remedy at law."325

To give a court of equity jurisdiction to enjoin ultra vires acts upon the part of a corporation at the suit of a stockholder, it is not necessary that there shall be any intentional wrong or actual fraud on the part of the officers or other stockholders. enough that the act is ultra vires. 326 Nor need there be any loss to the corporation. The fact that an ultra vires act or business will be beneficial to the corporation, and cannot injure its stockholders, makes it none the less ultra vires, and is no answer to a suit by a dissenting stockholder to enjoin the same.327

The clearest case in which a stockholder may sue to enjoin ultra vires acts or contracts of the directors or majority of the stockholders is where the act or contract will render the charter of the corporation subject to forfeiture in proceedings by the state, or otherwise tend to destroy the corporation. 328 But it is not at all necessary that it shall have this effect. A stockholder is entitled to relief against any diversion of the assets of the corporation to a purpose which is beyond the powers conferred upon it by its charter, or any unauthorized surrender of rights, etc. For example, a stockholder in a corporation created for the purpose of maintaining a toll bridge may sue to enjoin a majority of the stockholders from opening the bridge to the public as a free bridge, and ceasing to demand toll. 329 A stockholder in a railroad company may sue to enjoin the extension of its road

225 Mr. Justice Wayne, in Dodge 40 App. Div. (N. Y.) 424; ante, § v. Woolsey, 18 How. (U. S.) 331, 1 125. Smith's Cas. 257, 2 Keener's Cas. 228 Rendall v. Crystal Palace 257, 1 Cum. Cas. 739. See, also, Co., 4 Kay & J. 326; Stewart v. Marsh v. Eastern R. Co., 40 N. H. Erie & Western Transp. Co., 17 548, 77 Am. Dec. 732.

326 March v. Eastern R. Co., 43 N. H. 515, and other cases cited in note 323, supra.

<sup>327</sup> Byrne v. Schuyler Electric Works, 52 Ind.
 Mfg. Co., 65 Conn. 336; Davis v.
 Congregation Beth Tephila Israel, gle, 58 Ga. 474.

ley R. Co., 12 Blatchf. 280, Fed. Cas. No. 11,265; Manderson v. Commercial Bank, 28 Pa. St. 379; Rogers v. Lafayette Agricultural Works, 52 Ind. 304.

329 East Rome Town Co. v. Na-

beyond the terminus fixed by its charter. 330 A stockholder in a manufacturing corporation may sue to enjoin it from removing its plant and business to another state, where its charter requires the same to be located and carried on within the state.331 stockholder in any corporation may sue to enjoin its officers and majority of the stockholders from engaging in a line of business which is not authorized by its charter, however beneficial and profitable it may be;332 from carrying out ultra vires contracts;333 from making an ultra vires purchase of stock in another corporation; 334 from purchasing its own stock from certain stockholders, and paying therefor out of the assets of the corporation: 335 to declare void and set aside ultra vires bonds and a mortgage securing the same; 336 to set aside an illegal or fraudulent assignment by the directors in contemplation of insolvency;337 to enjoin a transfer of all the corporate property and the execution of all the corporate trusts to third persons;338 to enjoin a sale or lease of all the property of the corporation and abandonment of its business, where such action is not demanded by the exigencies of its business or the condition of its affairs;339

331 Stickle v. Liberty Cycle Co. (N. J. Eq.) 32 Atl. 708.

332 Cherokee Iron Co. v. Jones, 52 Ga. 276. And see generally ante, § 123 et seq.

333 Byrne v. Schuyler Electric Mfg. Co., 65 Conn. 336; Carson v. Iowa City Gaslight Co., 80 Iowa, 638. See ante, § 167 et seq.

334 Central R. Co. v. Collins, 40 Ga. 582, 1 Keener's Cas. 706. See ante, § 193 et seq.

335 Lowe v. Pioneer Threshing Co., 70 Fed. 646. See ante, § 199 et

836 City of Chicago v. Cameron,

Y.) 419.

Eq. Cas. (Pa.) 64.

389 Zabriskie v. Hackensack & New York R. Co., 18 N. J. Eq. 178,

330 Stevens v. Rutland & Bur- 90 Am. Dec. 617; Small v. Minnelington R. Co., 29 Vt. 545. apolis Electro-Matrix Co., 45 Minn. 264; Elyton Land Co. v. Dowdell, 113 Ala. 177, 59 Am. St. Rep. 105; Morris v. Elyton Land Co., 125 Ala. 263; Eldred v. American Palace-Car Co., 96 Fed. 59; Metcalf v. American School-Furniture Co., 108 Fed. 909; Forrester v. Boston & Montana Consolidated Copper & Silver Mining Co., 21 Mont. 544; Flynn v. Brooklyn City R. Co., 9 App. Div. 269, 158 N. Y. 493. And see post, chapter xxiv. Compare post, § 544. And see ante, § 160.

The fact that the value of the

shares of a stockholder who has not consented to an ultra vires 22 Ill. App. 91, 120 Ill. 447. transfer by the corporation to an337 Smith v. New York Consolidated Stage Co., 18 Abb. Pr. (N. dered to him, or deposited in court for him, does not defeat his right 2338 Langolf v. Seiberlitch, 2 Pars. to commence or continue a suit to enjoin or set aside the transfer. Morris v. Elyton Land Co., 125 Ala.

to enjoin acceptance of or action under an act of the legislature fundamentally altering or amending the charter of the corporation;340 to enjoin an unauthorized consolidation with another corporation;341 to enjoin the payment of dividends when there are no surplus profits available for the purpose;342 to cancel stock issued illegally or fraudulently, and to enjoin the holders thereof from voting at corporate meetings.343

In order that a person may sue as a stockholder of a corporation to enjoin its directors from engaging in a particular transaction or business, the transaction or business must be in violation of his rights as a stockholder. A person who is a stockholder in two corporations cannot sue to enjoin one of them from engaging in a business, on the ground that it is an illegal interference with the business of the other, and will therefore expose it to vexatious and expensive litigation, and thus diminish the value of his stock.844 A stockholder cannot sue to have declared null and void certain by-laws of the corporation, on the ground that, through their influence on persons sustaining business relations with him, they may cause him trouble and loss.345

A mere promise by a corporation to a subscriber for its stock not to engage in a particular business does not entitle him to enjoin its engaging in such business, if it is within the powers conferred upon it by its charter.346

340 Zabriskie v. Hackensack & Y.) 424. See ante, § 349 et seq., and New York R. Co., 18 N. J. Eq. 178, 90 Am. Dec. 617, 2 Smith's Cas. 760, 2 Keener's Cas. 1487, 1 Cum. Cas. 781; Kean v. Johnson, 9 N. J. Eq. 401, 1 Keener's Cas. 608; Stevens v. Rutland & Burlington R. Co., 29 Vt. 545, 1 Smith's Cas. 233; Witter v. Mississippi Quachita & Parsons v. Joseph, 92 Ala. 403, 1 Witter v. Mississippi, Ouachita & R. R. R. Co., 20 Ark. 463; Bove v. Junction R. Co., 10 Ind. 93; Academy of Music v. Flanders, 75 Ga. 14. See ante, § 482; post, chapter xxiv.

841 Nathan v. Tompkins, 82 Ala.
 437; Davis v. Congregation Beth
 Tephila Israel, 40 App. Div. (N.

Church Building Ass'n, 63 Wis. 9; Parsons v. Joseph, 92 Ala. 403, 1 Smith's Cas. 311, 2 Keener's Cas. 1653; Perry v. Tuskaloosa Cotton Seed Oil Mill Co., 93 Ala. 364.

344 Converse v. Hood, 149 Mass.

<sup>345</sup> Thomas v. Musical Mutual Protective Union, 121 N. Y. 45.

346 Converse v. Hood, 149 Mass.

#### § 540. Suits for redress or relief in case of fraud of the majority of stockholders.

It frequently happens that persons who own a majority of the stock of a corporation, and thus elect and control the directors or other officers, take advantage of their position to enter into contracts with the corporation through its directors or other officers for their own benefit, and in fraud of the stockholders, or to obtain possession of and appropriate its assets to their own use. In such a case, while the injury is, in legal contemplation, an injury to the corporation, it is clear that the minority stockholders would be absolutely without remedy, and helpless, if they were compelled to seek relief or redress through the corporation; and it is well settled, therefore, that any stockholder may sue in equity on his own behalf, and on behalf of the other stockholders not participating in the fraud, to enjoin the majority, or to set the fraudulent contract or transaction aside, and compel restoration.347

This principle applies where a majority of the stock in a corporation is acquired by another corporation, and the latter takes advantage of its position to obtain an inequitable lease or other

R. 5 Eq. 464, note, 1 Smith's Cas. 273, 1 Cum. Cas. 717; Menier v. Hooper's Telegraph Works, 9 Ch. App. 350, 1 Smith's Cas. 287, 1 Cum. Cas. 722; Ervin v. Oregon Railway & Navigation Co., 20 Fed. 577, 27 Fed. 625; Meeker v. Win-Co., 91 Fed. 940; Eldred v. Amerithrop Iron Co., 17 Fed. 48; Earle can Palace-Car Co., 96 Fed. 59; Dev. Seattle, Lake Shore & E. Ry. catur Mineral Land Co. v. Palm, Co., 56 Fed. 909; Rothwell v. Rob-113 Ala. 531, 59 Am. St. Rep. 140; inson, 39 Minn. 1, 12 Am. St. Rep. Jasper Land Co. v. Wallis, 123 Ala. 608; Woodroof v. Howes, 88 Cal. 652; Exter v. Sawyer, 146 Mo. 302; Erie & W. R. Co., 72 Hun (N. Y.)

Strip & W. R. Co., 72 Hun (N. Y.)

Strip & W. R. Co., 72 Hun (N. Y.)

Construction Co., 41 Neb. 574,

Strip & W. R. Co., 72 Hun (N. Y.)

Trimble v. American Sugar-RefinBarb. (N. Y.) 131; Currier v. New ing Co. (N. J. Ch.) 48 Atl. 912;

York, West Shore & B. R. Co., 35

Cross v. Johnson, 20 Wash. 124;

Gerry v. Bismarck Bank, 19 Mont.

Construction Co., 41 Neb. 574,

Strip & W. Salt River Valley 96 Pa. St. 253; Davis v. Gemmell, 191; Henshaw v. Salt River Valley 73 Md. 530; Sears v. Hotchkiss, 25 Canal Co. (Ariz.) 54 Pac. 577. And Conn. 171, 65 Am. Dec. 557; Hanley v. Balch, 94 Mich. 315; Chicago infra.

347 Atwood v. Merryweather, L. Hansom Cab Co. v. Yerkes, 141 Ill. 320, 33 Am. St. Rep. 315; Knoop v. Bohmrich, 49 N. J. Eq. 82; Bohmrich v. Knoop, 50 N. J. Eq. 585; Fougeray v. Cord, 50 N. J. Eq. 185; Wilcox v. Bickel, 11 Neb. 154. See, also, Weir v. Bay State Gas see the cases cited in note 353, contract from the former. In such a case, a dissenting stock-holder of the former may sue in equity in behalf of himself and other stockholders to set the contract aside, and compel restoration, and for other appropriate relief.<sup>348</sup>

Where one corporation acquires a majority of the stock of another corporation, and the two have substantially the same field of operation, so that the profits of one may be enhanced by a diminution of those of the other, or where there is a conflict of interest between the two in the matter of expenditures or in the division of earnings, the corporation owning the majority of the stock in the other, its agents and employes, and all other persons acting in its interest, may be enjoined from voting the stock in the election of officers of the other corporation, or from exercising the power which a majority of stock confers in controlling and governing such corporation.<sup>349</sup>

If certificates of stock are illegally issued, a stockholder may sue to cancel them and enjoin the holders from voting the same.<sup>350</sup>

# § 541. Suits for redress or relief in case of fraud, excess of authority, or negligence of directors or other officers.

If the directors or other officers of a corporation exceed their authority, not under an honest mistake, or are guilty of fraud or negligence in the management of the affairs of the corporation, threatening or causing loss to the corporation, the corporation, by action of the majority, may remove them, and may sue them for redress.<sup>351</sup> In such a case, the right to remove them and to sue for redress is in the corporation, for the injury is to the stockholders collectively, and individual stockholders cannot maintain a suit for relief or redress, unless for some rea-

348 Meeker v. Winthrop Iron Co., 17 Fed. 48; Earle v. Seattle, Lake Shore & E. Ry. Co., 56 Fed. 909; Pearson v. Concord R. Corp., 62 N. H. 537, 13 Am. St. Rep. 590; George v. Central Railroad & Banking Co., 1(1 Ala. 607. 349 Memphis & Charleston R.

Co. v. Woods, 88 Aka. 630, 16 Am. St. Rep. 81; George v. Central Railroad & Banking Co., 101 Ala. 607. See post, § 653(m).

350 Wood v. Union Gospel Church Building Ass'n, 63 Wis. 9.
351 Post, chapter xxiv.

son it cannot be obtained through the corporation. 352 If for any reason, however, relief or redress cannot be obtained through the corporation, as where the guilty directors own a majority of the stock, or the majority of the stockholders approve of or acquiesce in the fraud or mismanagement, or will not sue or take other steps to prevent the same, or hold the directors liable, or wherethere is no time to obtain action by the stockholders, any stockholder may obtain appropriate relief for the benefit of the corporation by a suit in equity on behalf of himself and other stockholders. The suit may be maintained under such circumstances in any case in which it appears that the directors or other officers are exceeding their authority by engaging in transactions which are beyond the powers conferred upon the corporation by its charter, or that, by making fraudulent contracts in the name of the corporation, or otherwise, they are or have been fraudulently managing the affairs of the corporation in their own interest, or in the interest of any other person than the corporation and its stockholders, or that they are converting or have converted the assets of the corporation to their own use, or that they have neglected or are neglecting their duty, to the injury of the corporation. And the suit may be either to enjoin or remove them, or to compel them to account or make good the loss to the corporation, or both. 353 The powers and duties of the directors and other officers of a corporation, and their liability for fraud,

352 Post, § 543. 253 England: Atwool v. Merry-weather, L. R. 5 Eq. 464, note, 1 Smith's Cas. 273, 1 Cum. Cas. 717; Menier v. Hooper's Telegraph Morks, 9 Ch. App. 350, 1 Smith's Cotton Seed Oil Mill Co., 93 Ala. Cas. 287, 1 Cum. Cas. 722; Salomons v. Laing, 12 Beav. 339, 14 Banking Co., 101 Ala. 607; Bell v. Jur. 279, 471; Mason v. Harris, 11 Montgomery Light Co., 103 Ala. Ch. Div. 97, 2 Keener's Cas. 1639, 1 Cum. Cas. 731; Gregory v. Patch-Palm, 113 Ala. 531, 59 Am. St. Rep. ett, 33 Beav. 595.

55, 74 Fed. 321; Earle v. Seattle, Lake Shore & E. Ry. Co., 56 Fed. 909; Weir v. Bay State Gas Co., 91 Fed. 940.

United States: Pond v. Vermont Valley R. Co., 12 Blatchf. 145, 76 Am. Dec. 508; Wright v. 280, Fed. Cas. No. 11,265; Ranger v. Champion Cotton-Press Co., 52 Co., 40 Cal. 20; Beach v. Cooper, Fed. 611; Excelsior Pebble Phosphate Co. v. Brown, 42 U. S. App. 101 Cal. 90; Ashton v. Dashaway

ultra vires acts, and negligence, will be considered in a subsequent chapter.<sup>354</sup>

Where the directors of a corporation wrongfully refuse to call a meeting of stockholders for the election of new directors, and a meeting cannot be called in any other way, a stockholder may sue in equity in behalf of himself and other stockholders,<sup>356</sup>

Ass'n, 84 Cal. 61; Woodroof v. Howes 88 Ala. 184; Moyle v. Landers (Cal.) 21 Pac. 1133; Smith v. Dorn, 96 Cal. 73.

Connecticut: Sears v. Hotchkiss, 25 Conn. 171, 65 Am. Dec. 557. Georgia: Colquitt v. Howard, 11

Ga. 556.

Illinois: City of Chicago v. Cameron, 120 Ill. 447; Harding v. American Glucose Co., 182 Ill. 551, 74 Am. St. Rep. 189; Chicago Hansom Cab Co. v. Yerkes, 141 Ill. 320, 33 Am. St. Rep. 315.

Iowa: Schoening v. Schwenk

(Iowa) 84 N. W. 916.

Maryland: Davis v. Gemmell, 73 Md. 530.

Massachusetts: Peabody v. Flint, 6 Allen, 52, 1 Smith's Cas. 263, 1 Cum. Cas. 795.

Michigan: Hanley v. Balch, 94 Mich. 315.

Minnesota: Rothwell v. Robinson, 39 Minn. 1, 12 Am. St. Rep. 608.

Missouri: Hannerty v. Standard Theater Co., 109 Mo. 297; Exter v. Sawyer, 146 Mo. 302.

Montana: Gerry v. Bismarck

Bank, 19 Mont. 191.

Nebraska: Wilcox v. Bickel, 11. Neb. 154; Fitzgerald v. Fitzgerald & Mallory Construction Co., 41 Neb. 374.

New Hampshire: March v. Eastern R. Co., 40 N. H. 548, 77 Am. Dec. 732; Id., 43 N. H. 515; Winsor v. Bailey, 55 N. H. 218, 1 Smith's Cas. 310; Pearson v. Concord R. Corp., 62 N. H. 537, 13 Am. Rep. 590.

New Jersey: Brown v. Vandyke, 8 N. J. Eq. 795, 55 Am. Dec. 250; Fougeray v. Cord, 50 N. J. Eq. 185; Wildes v. Rural Homestead Co., 53 N. J. Eq. 425.

New York: Robinson v. Smith,

3 Paige (N. Y.) 222, 24 Am. Dec. 212; Butts v. Wood, 37 N. Y. 317; Greaves v. Gouge, 69 N. Y.154; Barr v. New York, Lake Erie & W. R. Co., 96 N. Y. 444; Dyckman v. Valiente, 43 Barb. (N. Y.) 131; Gray v. New York & Virginia Steamship Co., 3 Hun (N. Y.) 383; Ithaca Gaslight Co. v. Treman, 30 Hun (N. Y.) 212; Carpenter v. Roberts, 56 How. Pr. (N. Y.) 216; Sheridan v. Sheridan Electric Light Co., 38 Hun (N. Y.) 396; Bloom v. National United Benefit Savings & Loan Co., 81 Hun (N. Y.) 120.

Ohio: Taylor v. Miami Export-

Ohio: Taylor v. Miami Exporting Co., 5 Ohio, 162, 22 Am. Dec.

Pennsylvania: Langolf v. Seiberlitch, 2 Pars. Eq. Cas. 64.

Rhode Island: Hodges v. New England Screw Co., 1 R. I. 312, 53 Am. Dec. 624; Hazard v. Durant, 11 R. I. 195.

South Dakota: Loftus v. Farmers' Shipping Ass'n, 8 S. D. 201.

Tennessee: Deaderick v. Wilson, 8 Baxt. 108; Wallace v. Lincoln Savings Bank, 89 Tenn. 630, 24 Am. St. Rep. 625.

Texas: Mussina v. Goldthwaite, 34 Tex. 125, 7 Am. Rep. 281; Cates v. Sparkman & Wise County Coal Co., 73 Tex. 619, 15 Am. St. Rep. 806; Becker v. Gulf City Street Railway & Real Estate Co., 80 Tex. 475.

Washington: Cross v. Johnson, 20 Wash. 124.

Wisconsin: Eschweiler v. Stowell, 78 Wis. 316, 23 Am. St. Rep.

354 See post, chapter xxiv.

<sup>355</sup> Pond v. Vermont Valley R. Co., 12 Blatchf. 280, Fed. Cas. No. 11,265; Lehigh Coal & Navigation Co. v. Central R. Co., 35 N. J. Eq. 349.

unless there is an adequate remedy at law by writ of mandamus. 356

Decree for payment directly to stockholders.—It has been held in effect that, where corporate funds have been misapplied, instead of being distributed as dividends, as in the fraudulent payment of excessive salaries to certain stockholders, and suit is brought in equity by injured stockholders to compel an accounting both with the company and with the complainants, the court may, by its decree, compel the payment directly to the complainants of their share of the moneys misappropriated, instead of decreeing repayment into the corporate treasury, and making it probably necessary for the complainants to resort to another suit to compel the payment of a dividend.<sup>357</sup>

# § 542. Suits against third persons to enjoin or redress injuries to the corporation.

If third persons, whether individuals or other corporations, or public officers, threaten to commit a wrong against the corporation, or have committed a wrong for which they are liable to the corporation in damages, or if a corporation has a right of action against another to enforce a contract or recover damages for its breach, or to recover property,—in all these cases, the injury to be prevented or redressed is an injury to the corporation, and not to the stockholders individually, except indirectly, and ordinarily the corporation is the only proper party to sue.358 The stockholders, however, are indirectly injured, and are entitled to relief in equity, for the protection of their equitable rights, if for any reason they cannot obtain relief through the corporation. And it is well settled, therefore, that a stockholder may maintain a suit in equity for appropriate relief on behalf of himself and the other stockholders, for the benefit of the corporation, if the directors refuse to sue or take other steps to pre-

<sup>\*\*</sup>S56 See People v. Cummings, 72 see Brown v. De Young, 167 Ill.

N. Y. 433. And see post, chapter 549; Fougeray v. Cord, 50 N. J. Eq. 

\*\*xiv.\*\*
\*\*s57 Eaton v. Robinson, 19 R. I. 

\*\*185; Davis v. Gemmell, 73 Md. 530. 

\*\*358 See ante, §\$ 537, 538; post, § 

146, 2 Keener's Cas. 1662. And 

\*\*543.\*\*

vent or redress the injury,—their refusal not being a proper exercise of their discretion, 359—and if, for any reason, relief cannot be obtained through the action of the stockholders as a body. 360

Thus, a stockholder may sue under such circumstances to enjoin the collection or payment of an illegal tax, as where the statute imposing the tax is unconstitutional;361 or to enjoin another corporation (as in the case of railroad companies) from taking or using its property under an unconstitutional statute, or otherwise without right;362 or to enjoin any other injury against which a suit for injunction is a proper remedy.363 stockholder may also sue under such circumstances to compel performance of a lease or other contract;364 to recover money illegally paid by the directors to a stockholder, upon allowing him to withdraw;365 to recover damages for conversion of corporate property;366 to recover damages for negligence or fraud

359 See post, § 544. tus v. Farmers' Shipping Ass'n, 8 360 Atwool v. Merryweather, L. S. D. 201; and other cases more 359 See post, § 544. R. 5 Eq. 464, note, 1 Smith's Cas. 273, 1 Cum. Cas. 717; Dodge v. Woolsey, 18 How. (U. S.) 331, 1 Smith's Cas. 257, 2 Keener's Cas. 1605 1 Cum. 1605, 1 Cum. Cas. 739; Greenwood Keener's Cas. 1605, 1 Cum. Cas. v. Union Freight R. Co., 105 U. S. 739; Barnes v. Kornegay, 62 Fed. 13, 2 Smith's Cas. 720, 1 Keener's 671; Davenport v. Dows, 18 Wall. Cas. 192, 1 Cum. Cas. 538; Pond v. Vermont Valley R. Co., 12 Blatchf. Keener's Cas. 1631, 1 Cum. Cas. 280, Fed. Cas. No. 11,265; March v. 754; Forbes v. Gracey, Fed. Cas. Eastern R. Co., 40 N. H. 548, 77 No. 4,924; Foote v. Linck, 5 Mc-Am. Dec. 732; Id., 43 N. H. 515; Lean, 616, Fed. Cas. No. 4,913; Winsor v. Bailey, 55 N. H. 218; Pollock v. Farmers' Loan & Trust Fitzgerald v. Fitzgerald & Mallory Co., 157 U. S. 429. Construction Co., 41 Neb. 374; Carter v. Ford Plate Glass Co., 85 Ind. R. Co., 105 U. S. 13, 2 Smith's Cas. 180; Mottu v. Primrose, 23 Md. 720, 1 Keener's Cas. 192, 1 Cum. 482; Brewer v. Boston Theatre, Cas. 538; Weidenfeld v. Sugar 482; Brewer v. Boston Theatre, Cas. 538; Weidenfeld v. Sugar 104 Mass. 378; Barr v. New York, Run R. Co., 48 Fed. 615.

Lake Erie & W. R. Co., 96 N. Y.
444; Bloom v. National United 400, Fed. Cas. No. 12,288; Weiden-Benefit Savings & Loan Co., 81 feld v. Sugar Run R. Co., 48 Fed. Hun (N. Y.) 120; Currier v. New 615.

York, West Shore & B. R. Co. 25 York, West Shore & B. R. Co., 35 Hun (N. Y.) 355; Burbank v. Den-nis, 101 Cal, 90; Miller v. Murray, N. H. 515; Barr v. New York, Lake 17 Colo. 408; Hannerty v. Stan-dard Theater Co., 109 Mo. 297; 365 Melvin v. Lamar Ins. Co., 80 Exter v. Sawyer, 146 Mo. 302; Lof-111. 446, 22 Am. Rep. 199, 2 Smith's

specifically cited in the notes following.

361 Dodge v. Woolsey, 18 How. (U. S.) 331, 1 Smith's Cas. 257, 2 671; Davenport v. Dows, 18 Wall. (U. S.) 626, 1 Smith's Cas. 280, 2

362 Greenwood v. Union Freight

364 March v. Eastern R. Co., 40

resulting in injury to the corporation;367 to rescind and cancel a contract which the corporation has a right to avoid;368 to set aside a fraudulent contract between the promoters of the corporation and the directors, by which property is purchased from the promoters at an excessive valuation, or to compel the promoters or directors, or both, to account to the corporation for secret profits made by them in such a transaction: 369 to set aside an ultra vires or fraudulent lease or other conveyance of the property of the corporation; 370 to declare ultra vires and cancel bonds and a mortgage securing the same;371 and in many other cases.

#### Necessity for effort to obtain relief through the corpora-§ 543. tion or its officers.

The right of a stockholder to sue in equity to prevent or redress injuries to the corporation, as shown in the preceding sections, is not unlimited, but depends upon his inability to obtain relief through the corporation or its officers. The right to sue is primarily in the corporation; and in order that a stockholder may sue in his own name, he must show in his bill or complaint that he has made every reasonable effort, in good faith, to obtain relief within and through the corporation by requesting the directors or other officers to sue or take other proper steps, and, on their refusal to do so, by applying to the stockholders; or else he must show that such a request and application would be useless because the directors and majority of the stockholders are themselves

rens Lumber Co., 98 Ga. 329.

967 Colquitt v. Howard, 11 Ga.

366 Currier v. New York, West Shore & B. R. Co., 35 Hun (N. Y.) 355; City of Chicago v. Cameron, 120 Ill. 447, 22 Ill. App. 91; Loftus v. Farmers' Shipping Ass'n, 8 S. D. 201.

369 Atwool v. Merryweather, L. 22 III. App. 91, 120 III. 447.

Cas. 852, 2 Keener's Cas. 1197. See R. 5 Eq. 464, note, 1 Smith's Cas. ante, § 476. 273, 1 Cum. Cas. 717; Burbank v. 366 Steele Lumber Co. v. Lau Dennis, 101 Cal. 90; Exter v. Saw-

yer, 146 Mo. 302.
Compare Foss v. Harbottle, 2
Hare, 461, 1 Smith's Cas. 267, 2
Keener's Cas. 1588, 1 Cum. Cas.

693. See ante, § 110.
370 Wilcox v. Bickel, 11 Neb.
154; People's Savings Bank v. Colorado Mining Exchange Building Co., 8 Colo. App. 354.

371 City of Chicago v. Cameron,

guilty of the wrongs complained of, or because the directors refuse to act, or are guilty of the wrongs, and there is no time or power to call a meeting of the stockholders, or because the majority of the stockholders are parties to or approve the wrongs, etc. Without such a showing as this, a bill or complaint by a stockholder, where the injury is to the corporation, is demurrable.372 It must appear not merely that the directors or other managing officers are parties to the frauds or other wrongs

2 Hare, 461, 1 Smith's Cas. 267, 2 Keener's Cas. 1538, 1 Cum. Cas. 693; Mozley v. Alston, 1 Phil. Ch. 800; Russell v. Wakefield Waterworks Co., L. R. 20 Eq. 474, 1 Smith's Cas. 291, 1 Cum. Cas. 725; Gray v. Lewis, 8 Ch. App. 1050.

United States: Dodge v. Woolsey, 18 How. 331, 1 Smith's Cas. 257, 2 Keener's Cas. 1605, 1 Cum. Cas. 739; Hawes v. Oakland, 104 U. S. 450, 1 Smith's Cas. 282, 2 Keener's Cas. 1647, 1 Cum. Cas. 756; Detroit v. Dean, 106 U.S. 537; Dimpfell v. Ohio & Mississippi Ry. Co., 110 U.S. 209, 1 Cum. Cas. 765; Allen v. Wilson, 28 Fed. 677; Daunmeyer v. Coleman, 11 Fed. 97; Taylor v. Holmes, 14 Fed. 498; McGeorge v. Big Stone Gap Improvement Co., 57 Fed. 262; Putnam v. Ruch, 54 Fed. 216, 56 Fed. 416; Bill v. Western Union Telegraph Co., 16 Fed. 14; Foote v. Cunard Mining Co., 17 Fed. 46. And see post, § 550. Alabama: Merchants' & Plant-

ers' Line v. Waganer, 71 Ala. 581; Mack v. De Bardeleben Coal & Iron Co., 90 Ala. 396; Memphis & Charleston R. Co. v. Woods, 88 Ala. 630, 16 Am. St. Rep. 81; Bell v. Montgomery Light Co., 103 Ala. 275; Decatur Mineral Land Co. v. Palm, 113 Ala. 531, 59 Am. St. Rep. 140; Johnson v. National Building & Loan Ass'n, 125 Ala. 465; Louisville & Nashville R. Co. v. Neal

(Ala.) 29 South, 865.

California: Bacon v. Irvine, 70 Cal. 221; Cogswell v. Bull, 39 Cal. 320; Ashton v. Dashaway Ass'n, 84 Cal. 61; Woodroof v. Howes, 88 Cal. 184; Moyle v. Landers' Adm'r,

872 England: Foss v Harbottle, 83 Cal. 579; Waymire v. San Francisco & San Mateo Ry. Co., 112 Cal. 646.

Colorado: Miller v. Murray, 17 Colo. 408.

Georgia: Henry v. Elder, 63 Ga. 347; Ware v. Bazemore, 58 Ga. 316; Alexander v. Searcy, 81 Ga. 536, 12 Am. St. Rep. 337; Steele Lumber Co. v. Laurens Lumber Co., 98 Ga.

Iowa: Dillon v. Lee, 110 Iowa, 156.

Kansas: Atchison, Topeka & Santa Fe R. Co. v. Sumner County. 51 Kan. 617; Home Mining Co. v. McKibben, 60 Kan. 387.

Kentucky: Shawhan v. Zinn, 79 Ky. 300.

Maine: Hérsey v. Veazie, 24 Me. 9, 41 Am. Dec. 364; Smith v. Poor, 40 Me. 415, 63 Am. Dec. 672; Kennebec & Portland R. Co. v. Portland & Kennebec R. Co., 54 Me. 173; Ulmer v. Maine Real Estate Co., 93 Me. 324.

Maryland: Booth v. Robinson, 55 Md. 419.

Massachusetts: Brewer v. Boston Theatre, 104 Mass. 378; Dunphy v. Traveller Newspaper Ass'n, 146 Mass. 495, 1 Cum. Cas. 769; Warren v. Para Rubber Shoe Co., 166 Mass. 97.

Michigan: Talbot v. Scripps, 31 Mich. 268.

Minnesota: Mealey v. Nickerson, 44 Minn. 430; Morrill v. Little Falls Mfg. Co., 46 Minn. 260; Hodg-son v. Duluth, Huron & D. R. Co., 46 Minn. 454.

New Jersey: Brown v. Vandyke, 8 N. J. Eq. 795, 55 Am. Dec. 250. New York: Robinson v. Smith,

complained of, or that they cannot or will not sue for redress, or take other proper action to remedy the same, but also that redress or relief cannot be obtained at all or in time by application to and action by the stockholders, who have the power to control the directors or managing officers, or to remove them and appoint others in their place, who will take proper action; or else it must be shown that the majority of the stockholders are in collusion

3 Paige, 222, 24 Am. Dec. 212; Forbes v. Whitlock, 3 Edw. Ch. 446; Greaves v. Gouge, 69 N. Y. 154; Barr v. New York, Lake Erie & W. R. Co., 125 N. Y. 263; Vanderbilt v. Garrison, 3 Abb. Pr. 361; House v. Cooper, 30 Barb. 157, 16 How. Pr. 292; Flynn v. Brooklyn City R. Co., 9 App. Div. 269, 158 N. Y. 493; Fitchett v. Murphy, 46 App. Div. (N. Y.) 181, reversing 26 Misc. Rep. 544; Corning v. Barrett, 22 Misc. Rep. 241.

North Carolina: Moore v. Silver Valley Mining Co., 104 N. C. 534.

Pennsylvania: Holton v. New Castle Ry. Co., 138 Pa. St. 111; South West Natural Gas Co. v. Fayette Fuel-Gas Co., 145 Pa. St. 13; Wolf v. Pennsylvania R. Co., 195 Pa. St. 91.

Rhode Island: Hazard v. Durant, 11 R. I. 195.

South Carolina: Latimer v. Richmond & Danville R. Co., 39 S. C. 44; Wenzel v. Palmetto Brewing Co., 48 S. C. 80.

Tennessee: Black v. Huggins, 2 Tenn. Ch. 780; Deaderick v. Wilson, 8 Baxt. 108; Boyd v. Sims, 87 Tenn. 771; Wallace v. Lincoln Savings Bank, 89 Tenn. 630, 24 Am. St. Rep. 625.

Texas: Cates v. Sparkman & Wise County Coal Co., 73 Tex. 619, 15 Am. St. Rep. 806.

Virginia: Mount v. Radford Trust Co., 93 Va. 427.

West Virginia: Rathbone v. Parkersburg Gas Co., 31 W. Va. 798; Park v. Ulster & Kanawha Petroleum Co., 25 W. Va. 108.

Wisconsin: Doud v. Wisconsin, Pittsville & S. Ry. Co., 65 Wis. 108, 56 Am. Rep. 620.

"The decisions are clear and pointed, fully establishing the doctrine that a stockholder has not the right to bring an action in his own name against officers of a corporation for fraudulent acts or waste of the corporate property, unless such corporation, or its officers, upon being applied to for such purpose by the stockholder, refuses to prosecute, or unless it appears that a request to prosecute would be useless." Doud v. Wisconsin, Pittsville & S. Ry. Co., 65 Wis. 108, 56 Am. Rep. 620.

After a receiver, with power to sue, has been appointed under a statute for the purpose of winding up a corporation, a stockholder cannot maintain a separate suit against the directors for misappropriation of corporate funds by them. His remedy is by petition to the receiver or to the court for the institution of an action. Cunningham v. Wechselberg, 105 Wis. 359.

That the objection that the plaintiff made no effort to obtain relief within or through the corporation goes to his capacity to sue, and is waived if not raised by demurrer, see Wood v. Union Gospel Church Building Ass'n, 63 Wis. 9.

Stockholders suing to redress an injury to the corporation are not entitled to recover if their allegation that they requested the corporation to institute suit, and it refused, is denied and not proved. Dillon v. Lee, 110 Iowa, 156.

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with the guilty officers, or that, for some other reason, an effort to obtain relief through them would be useless.<sup>373</sup>

A request or demand upon the directors or majority of the stockholders to bring suit or take other steps to obtain relief need not be made by a stockholder before suing in his own behalf, if the circumstances are such as to clearly show that it would be a mere useless form. No such request or demand is necessary, therefore, as a general rule, where the wrong complained of was done or is threatened by a majority of the stockholders, or by the directors with the consent or approval of a majority of the stockholders, or by an officer who himself owns a majority of the stock.374 Where the stockholders of a corporation have no con-

373 Mozley v. Alston, 1 Phil. Ch. 800; Foss v. Harbottle, 2 Hare, 461. 1 Smith's Cas. 267, 2 Keener's Cas. 1 Smtth's Cas. 261, 2 Reener's Cas. 1588, 1 Cum. Cas. 693; Hawes v. Oakland, 104 U. S. 450, 1 Smith's Cas. 282, 2 Keener's Cas. 1647, 1 Cum. Cas. 756; McMurray v. Northern Ry. Co., 22 Grant Ch. (Can.) 476; Rathbone v. Parkersburg Gas Co., 31 W. Va. 798; Doud v. Wis-consin, Pittsville & S. Ry. Co., 65 Wis. 108, 56 Am. Rep. 620; Tuscaloosa Mfg. Co. v. Cox, 68 Ala. 71; and other cases cited in note 372,

supra.

374 United States: Heath v. Erie
Ry. Co., 8 Blatchf. 347, Fed. Cas.
No. 6,306; Sellers v. Phoenix Iron
Co., 13 Fed. 20; Excelsior Pebble
Phosphate Co. v. Brown, 42 U. S.
App. 55, 74 Fed. 321; Earle v. Seattle, Lake Shore & E. Ry. Co., 56
Fed. 909; County of Tazewell v.
Farmers' Loan & Trust Co., 12 Fed.
752; Rogers v. Nashville, Chattanooga & St. L. Ry. Co. (C. C. A.)
91 Fed. 299; Barcus v. Gates (C. C.
A.) 89 Fed. 783; Weir v. Bay State
Gas Co., 91 Fed. 940.
Alabama: Nathan v. Tompkins.

Alabama: Nathan v. Tompkins, 82 Ala. 437; Mack v. De Bardele-ben Coal & Iron Co., 90 Ala. 396; George v. Central Railroad & Banking Co., 101 Ala. 607; Bell v. Montgomery Light Co., 103 Ala. 275; Jasper Land Co. v. Wallis, 123 Ala. 652.

California: Moyle v. Landers, 21 Pac. 1133; Smith v. Dorn, 96 Cal. 73; Wickersham v. Crittenden, 106 Cal. 329; Shively v. Eureka Tellurium Gold Mining Co., 129 Cal. 293.

Colorado: Miller v. Murray, 17

Colo. 408.

Connecticut: Starbuck v. Mercantile Trust Co., 60 Conn. 553.

Illinois: City of Chicago v. Cameron, 120 Ill. 447; Green v. Hedenberg, 159 Ill. 489, 50 Am. St. Rep. 178; Harding v. American Glucose Co., 182 Ill. 551, 628, 74 Am. St. Rep. 189, 223; Stebbins v. Perry County, 167 Ill. 567.

Schoening v. Schwenk (Iowa) 84 N. W. 916. Compare Dillon v. Lee, 110 Iowa, 156.

Massachusetts: Brewer v. Boston Theatre, 104 Mass. 378; Blair v. Telegram Newspaper Co., 172 Mass. 201.

Minnesota: Rothwell v. Robinson, 39 Minn. 1, 12 Am. St. Rep. 608; Pencille v. State Farmers' Mutual Hail Ins. Co., 74 Minn. 67, 73 Am. St. Rep. 326.

Missouri: Hannerty v. Standard Theater Co., 109 Mo. 297.

Montana: Gerry v. Bismarck Bank, 19 Mont. 191.

New Jersey: Knoop v. Bohmrich, 49 N. J. Eq. 82; Bohmrich v. Knoop, 50 N. J. Eq. 485.

New York: Currier v. New York,

trol of its business except through an annual election of officers, a refusal of those officers to sue is sufficient to authorize a suit by a stockholder.375 Where a corporation has ceased to appoint officers, and has abandoned its business, a stockholder may sue for himself and others for the protection of their rights, without showing or alleging a refusal of corporate officers to act. 376

Although a request upon the directors or other governing body of a corporation by a stockholder for redress of grievances

West Shore & B. R. Co., 35 Hun, 355; Meyers v. Scott, 50 Hun, 603; Davis v. Congregation Beth Tephila Bavis V. Conglegation Beth Tephnia Israel, 40 App. Div. (N. Y.) 424; Walter v. F. E. McAlister Co., 21 Misc. Rep. (N. Y.) 747; Lewisohn Bros. v. Anaconda Copper Mining Co., 23 Misc. Rep. (N. Y.) 31.

south Carolina: Stahn v. Catawba Mills, 53 S. C. 519.

South Dakota: Loftus v. Farmers' Shipping Ass'n, 8 S. D. 201. Tennessee: Tennessee Mountain Petroleum & Mining Co. v. Ayers (Tenn. Ch. App.) 43 S. W.

34 Tex. 125, 7 Am. Rep. 281.

West Virginia: Crumlish's Adm'r v. Shenandoah Valley R. Co., 28 W. Va. 623.

Wisconsin: Eschweiler v. Stowell, 78 Wis. 316, 23 Am. St. Rep.

"It is not necessary that the corporation should absolutely refuse by vote at the general meeting, if it can be shewn either that the wrong-doer had command of the majority of the votes, so that it would be absurd to call the meeting; or if it can be shewn that there has been a general meeting substantially approving of what has been done; or if it can be shewn from the acts of the corporation as a corporation, distinguished from the mere acts of the directors of it, that they have approved of what has been done, and have allowed a long time to elapse without interfering, so that they do not intend and are not willing to sue. In all those cases the same istence when the cause of action doctrine applies, and the individual arose. Dillon v. Lee, 110 Iowa, 156.

corporator may maintain the suit." Sir G. Jessel, M. R., in Russell v. Wakefield Waterworks Co., L. R. 20 Eq. 474, 1 Smith's Cas. 291, 1 Cum. Cas. 725.

In Stebbins v. Perry County, 167 Ill. 567, it was held that a stockholder might sue to cancel stock issued to a county for bonds unlawfully issued by the county, without having made a demand on the corporation to sue, as the corporation could not sue to cancel its own stock. And see Barcus v. Gates (C. C. A.) 89 Fed. 783.

An allegation that one of the de-

Texas: Mussina v. Goldthwaite, fendants guilty of the fraudulent or wrongful acts complained of is the president and treasurer of the corporation, and is, and for a long time has been, the owner or con-troller of a majority of the shares of stock, and by reason thereof has chosen the directors, etc., does not show sufficient excuse for failure of the complaining stockholder to apply to the directors to move in the interest of the corporation. Dunphy v. Traveller Newspaper Ass'n, 146 Mass. 495, 1 Cum. Cas. 769: Brewer v. Boston Theatre, 104 Mass. 378.

> 375 Brewer v. Boston Theatre, 104 Mass. 378.

> 376 Crumlish's Adm'r v. Shenandoah Valley R. Co., 28 W. Va. 623.

> It has been held that demand upon and refusal of a corporation to sue is not excused, so as to authorize a stockholder to sue, by the fact that the corporation has been dissolved, where it was in ex

§ 544a

before he sues is not necessary when the corporate management is in the control of the guilty parties, or for any other reason such a request would be fruitless, the bill or complaint must allege with particularity the facts which excuse such request.377

#### Discretionary powers of directors or majority of the stockholders.

(a) In general.—The doctrine that a stockholder may sue in equity to redress or prevent wrongs on the part of the directors or majority of the stockholders, or to obtain redress on behalf. of the corporation for injuries by strangers, where he cannot obtain relief through the corporation, does not give a stockholder the right to maintain such a bill where the act complained of, or the refusal of the directors or majority of the stockholders to sue, is properly within the discretionary power with respect to the internal affairs of the corporation vested in them by the charter. So long as they act, not fraudulently, illegally, or oppressively, but in good faith, in the exercise of their discretion, and for what they deem to be the best interests of the company, a court of equity has no jurisdiction to interfere at the suit of a dissenting stockholder, or a dissenting minority of the stockholders. Such a suit cannot be maintained by showing a mere mistake or error of judgment on the part of the directors or majority of the stockholders. Their conduct must be ultra vires, illegal, fraudulent, or oppressive.378

377 Bell v. Montgomery Light Co., 103 Ala. 275; Jasper Land Co. v. Wallis, 123 Ala. 652; Louisville & Nashville R. Co. v. Neal (Ala.) 29 So. 865; Flynn v. Brooklyn City R. Co., 9 App. Div. 269, 158 N. Y. 493. And see the federal cases drickson v. Bradley (C. C. A.) 85 cited post, § 550, and other cases Fed. 508; Ryan v. Williams, 100 cited in the notes preceding.

378 England: Foss v. Harbottle, 2 Hare, 461, 1 Smith's Cas. 267, 2 Keener's Cas. 1588, 1 Cum. Cas. 693; Macdougall v. Gardiner, 1 Ch.

United States: Samuel v. Holladay, Woolw. 400, Fed. Cas. No. 12,288; Bill v. Western Union Telegraph Co., 16 Fed. 14; Hayden v. Official Hotel Red Book & Directory Co., 42 Fed. 875; Hen-Fed. 172.

Alabama: Tuscaloosa Mfg. Co. v. Cox, 68 Ala. 71.

Pratt v. Pratt, Connecticut: 693; Macdougall v. Gardiner, 1 Ch. Read & Co., 33 Conn. 446, 2 Keen-Div. 13, 2 Keener's Cas. 1632, 1 er's Cas. 1421, 2 Cum. Cas. 219; Cum. Cas. 704. Town of Middletown v. Boston &

"Each and every stockholder," said the Kentucky court, "contracts that the will of the majority shall govern in all matters coming within the limits of the act of incorporation; and in cases involving no breach of trust, but only error or mistake of judgment upon the part of the directors who represent the company, individual stockholders have no right to appeal to the courts to dictate the line of policy to be pursued by the corporation."379 "Questions of policy of management, of expediency of contracts or action, of adequacy of consideration not grossly disproportionate, of lawful appropriation of corporate funds to advance corporate interests, are left solely to the honest decision of the directors if their powers are without limitation and free To hold otherwise would be to substitute the from restraint. judgment and discretion of others in the place of those determined on by the scheme of incorporation."380

Illinois: Wheeler v. Pullman Iron & Steel Co., 143 Ill. 197, affirming 43 Ill. App. 626.

Kentucky: Dudley v. Kentucky High-School, 9 Bush, 576, 2 Keener's Cas. 1629, 1 Cum. Cas. 767.

Maine: Inhabitants of Waldoborough v. Knox & Lincoln R. Co., 84 Me. 469; Kennebec & Portland R. Co. v. Portland & Kennebec R. Co., 54 Me. 173.

Shaw v. Davis, 78 Maryland: Md. 308.

Massachusetts: Durfee v. Old Colony & Fall River R. Co., 5 Allen, 230, 1 Smith's Cas. 750, 2 Keener's Cas. 1480, 1 Cum. Cas. 773; Dunphy v. Traveller Newspaper Ass'n, 146 Mass. 495, 1 Cum.

Minnesota: Rothwell v. Robin-

son, 44 Minn. 538.

Son, 44 Minn. 558.

New Jersey: Story v. Jersey
City & Bergen Point Plank Road
Co., 16 N. J. Eq. 13, 84 Am. Dec.
134; Sewell v. East Cape May
Beach Co., 50 N. J. Eq. 717; Gifford v. New Jersey R. & Transp.
Co., 10 N. J. Eq. 171; Ellerman
v. Chicago Junction Railways &

New York Air Line R. Co., 53 Conn. Union Stockyards Co., 49 N. J. Eq. 351. 217; Meredith v. New Jersey Zinc Georgia: Hand v. Dexter, 41 Ga. & Iron Co., 59 N. J. Eq. 257; Trimble v. American Sugar-Refining Co. (N. J. Ch.) 48 Atl. 912.

New York: Leslie v. Lorillard, 110 N. Y. 519, 1 Keener's Cas. 465; Hart v. Ogdensburg & Lake Champlain R. Co., 89 Hun, 316; Thompson v. Erie Ry. Co., 11 Abb. Pr. (N. S.) 188; Rafferty v. Buffalo City Gas Co., 37 App. Div. (N. Y.) 618; Lewisohn Bros. v. Anaconda Copper Mining Co., 26 Misc. Rep. (N. Y.) 613.

Pennsylvania: Lauman v. Lebanon Valley R. Co., 30 Pa. St. 42, 72 Am. Dec. 685.

Wallace v. Lincoln Tennessee: Savings Bank, 89 Tenn. 630, 24 Am. St. Rep. 625; Memphis Gayoso Gas Co. v. Williamson, 9 Heisk. 314.

Texas: Cates v. Sparkman & Wise County Coal Co., 73 Tex. 619, 15 Am. St. Rep. 806.

Virginia: Baltimore & Ohio R. Co. v. City of Wheeling, 13 Grat.

See, also, post, chapter xxiv. 379 Dudley v. Kentucky High-School, 9 Bush (Ky.) 576, 2 Keener's Cas. 1629, 1 Cum. Cas. 767.

880 Ellerman .v. Chicago Junction

In a leading English case it was said by James, L. J.: "Nothing connected with internal disputes between the shareholders is to be made the subject of a bill by some one shareholder on behalf of himself and others, unless there be something illegal. oppressive, or fraudulent—unless there is something ultra vires on the part of the company qua company, or on the part of the majority of the company, so that they are not fit persons to determine it; but \* \* \* every litigation must be in the name of the company, if the company really desire it. Because there may be a great many wrongs committed in a companythere may be claims against directors, there may be claims against officers, there may be claims against debtors; there may be a variety of things which a company may well be entitled to complain of, but which, as a matter of good sense, they do not think it right to make the subject of litigation; and it is the company, as a company, which has to determine whether it will make anything that is a wrong to the company a subjectmatter of litigation, or whether it will take steps itself to prevent the wrong from being done."381

(b) Illustrations.—In accordance with this well-established doctrine, it has been held that a stockholder cannot sue in behalf of himself and other stockholders to enjoin a sale of a part or all the property of the corporation, if the sale is not ultra vires, and there is no element of fraud; 382 to enjoin a sale of all the property of the corporation in good faith to another corporation engaged in the same business for paid-up stock in the latter, where the business of the corporation can no longer be carried on profitably, and it is approaching serious financial embarrassment;383 to enjoin a lease, which is within the powers of the

49 N. J. Eq. 217.

381 James, L. J., in Macdougall v. Gardiner, 1 Ch. Div. 13, 2 Keener's ley R. Co., 30 Pa. St. 42, 72 Am. Cas. 1632, 1 Cum. Cas. 704.

Point Plank Road Co., 16 N. J. Eq. 13; Lipton v. Bald Eagle Plank

388 Sawyer v. Dubuque Printing
Road Co., 17 Leg. Int. (Pa.) 365; Co., 77 Iowa, 242; Trisconi v. WinSewell v. East Cape May Beach Co., ship, 43 La. Ann. 45, 26 Am. St.

Railways & Union Stockyards Co., 50 N. J. Eq. 717; Hayden v. Official Hotel Red-Book & Directory Co., 42 Fed. 875. Lauman v. Lebanon Valas. 1632, 1 Cum. Cas. 704. Dec. 685; Hall v. City of Syracuse, 382 Story v. Jersey City & Bergen 71 Hun (N. Y.) 465. See, also, bint Plank Road Co., 16 N. J. Eq. ante, § 152 et seq.

corporation;384 to compel the directors to declare a dividend, where there is no abuse of discretion on their part in refusing to do so;385 or to enjoin acceptance of or acting under an alteration or amendment of the charter of the corporation, when its acceptance is within the discretion of a majority of the stockholders.386

A stockholder cannot maintain a bill in equity to set aside an act or transaction which was done irregularly or illegally, but which a majority of the stockholders are entitled to do regularly or legally.<sup>387</sup> Nor can a stockholder sue to set aside a transaction on the part of the directors on the ground that it was fraudulent, irregular, illegal, or in excess of the powers conferred upon the directors, where the transaction is within the powers of the corporation, and such, therefore, as a majority of the stockholders may ratify,388 unless, as may sometimes be the case, it is impossible to procure a meeting of the stockholders to pass upon the transaction.<sup>389</sup> This principle was applied in a leading English case, where a stockholder sued to set aside a purchase by the directors for the corporation of their own land. It was held that, while the transaction might be avoided by the corporation, it might also be ratified, and that the suit, therefore, could not be maintained without showing that no action of the stockholders could be obtained. "Whilst the court," said

384 Town of Middletown v. Boston & New York Air Line R. Co., 53 Conn. 351.

385 See ante, § 517(f).

386 Mowrey v. Indianapolis & Cincinnati R. Co., 4 Biss. 78, Fed. Cas. No. 9,891; Zabriskie v. Cleve-Hand, Columbus & C. R. Co., 23 How. (U. S.) 381; Durfee v. Old Colony & Fall River R. Co., 5 Al-Colony & Fall River R. Co., 5 Al1en (Mass.) 230, 1 Smith's Cas. 750, Cas. 1588, 1 Cum. Cas. 693; Bill v.
2 Keener's Cas. 1480, 1 Cum. Cas. Western Union Telegraph Co., 16
773; Sprigg v. Western Telegraph Fed. 14.
Co., 46 Md. 67; Sprague v. Illinois
River R. Co., 19 Ill. 174; Sage v.
1589; Foss v. Harbottle, 2 Hare, 461, 1889; Foss v

Rep. 175. And see ante, §§ 160, Co., 11 Mich. 155. See ante, § 482;

post, chapter xxiv.

387 Foss v. Harbottle, 2 Hare, 461, 1 Smith's Cas. 267, 2 Keener's Cas. 1588, 1 Cum. Cas. 693; Macdougall v. Gardiner, 1 Ch. Div. 13, 2 Keen-Cas. 1632, 1 Cum. Cas. 704; Dudley v. Kentucky High-School, 9 Bush (Ky.) 576, 2 Keener's Cas. 1629, 1 Cum. Cas. 767.

388 Foss v. Harbottle, 2 Hare, 461, 1 Smith's Cas. 267, 2 Keener's

Dillard, 15 B. Mon. (Ky.) 340; Joy 1588, 1 Cum. Cas. 693; Brewer v. v. Jackson & Michigan Plank Road Boston Theatre, 104 Mass. 378.

Vice Chancellor Wigram, "may be declaring the acts complained of to be void at the suit of the present plaintiffs, who in fact may be the only proprietors who disapprove of them, the governing body of proprietors may defeat the decree by lawfully resolving upon the confirmation of the very acts which are the subject of the suit. The very fact that the governing body of proprietors assembled at the special general meeting may so bind even a reluctant minority, is decisive to shew that the frame of this suit cannot be sustained whilst that body retains its functions. In order then that this suit may be sustained, it must be shewn either that there is no such power as I have supposed remaining in the proprietors, or, at least, that all means have been resorted to and found ineffectual to set that body in motion."390

A payment of funds of the corporation, or other act by the directors, which is conceded to be ultra vires, as the payment of a tax which is conceded to be illegal, but the payment of which the directors consider it inadvisable to resist, cannot be said to be due to a mere error of judgment.391

(c) Refusal to sue.—The mere fact that a corporation has a cause of action for an injury does not always make it incumbent upon it to sue, any more than in the case of an individual. If, in the opinion of the directors or a majority of the stockholders, the best interests of the company do not require it to sue, it need not do so. The matter is within their discretion, and if they act in good faith, their refusal to sue violates no right of dissenting stockholders, so as to entitle them to maintain a suit in their own behalf.392 "It would be contrary to the fundamental prin-

1588, 1 Cum. Cas. 693.

Keener's Cas. 1605, 1 Cum. Cas, 739. Fed. Cas. No. 12,288.

392 In re London & Mercantile Discount Co., L. R. 1 Eq. 277; Foss suit to set aside a judgment ob-

<sup>390</sup> Foss v. Harbottle, 2 Hare, 461, phy v. Traveller Newspaper Ass'n, 1 Smith's Cas. 267, 2 Keener's Cas. 146 Mass. 495, 1 Cum. Cas. 769; Wallace v. Lincoln Savings Bank, 391 Dodge v. Woolsey, 18 How. 89 Tenn. 630, 24 Am. St. Rep. 625;
 (U. S.) 331, 1 Smith's Cas. 257, 2 Samuel v. Holladay, Woolw. 400,

A stockholder cannot maintain a V. Harbottle, 2 Hare, 461, 1 Smith's tained against the corporation upon Cas. 267, 2 Keener's Cas. 1588, 1 allegations which show merely that Cum. Cas. 693; Macdougall v. Garthe corporation itself has declined diner, 1 Ch. Div. 13, 2 Keener's to bring the suit on the advice of Cas. 1632, 1 Cum. Cas. 704; Dunctum competent attorneys that it could ciples of corporate organization," said Judge Knowlton in a Massachusetts case, "to hold that a single shareholder can at any time launch the corporation into litigation to obtain from another what he deems to be due to it, or to prevent methods of management which he thinks unwise. Intelligent and honest men differ upon questions of business policy. It is not always best to insist upon all one's rights; and a corporation acting by its directors, or by vote of its members, may properly refuse to bring a suit which one of its stockholders believes should be prosecuted. In such a case the will of the majority must control. It is only when the action of a corporation in refusing to proceed at the request of a stockholder is fraudulent as against him, or in disregard of his rights, that he can maintain a suit in his own name in the corporate right. The court cannot interfere with the management of corporations in matters which are properly within their discretion, so long as their discretion is fairly exercised, and it is always assumed until the contrary appears, that they and their officers obey the law, and act in good faith towards all their members,"393

## § 545. Summary of the circumstances necessary to enable a stock-holder to sue.

In a leading case in the supreme court of the United States, the circumstances necessary to entitle a stockholder to sue in his own name were summed up by Mr. Justice Miller as follows:

"We understand the doctrine to be that to enable a stockholder in a corporation to sustain in a court of equity in his own name, a suit founded on a right of action existing in the corporation itself, and in which the corporation itself is the appropriate plaintiff, there must exist as the foundation of the suit—

"1. Some action or threatened action of the managing board of directors or trustees of the corporation which is beyond the authority conferred on them by their charter or other source of organization;

not be successful. Hendrickson v. 393 Dunphy v. Traveller News-Bradley (C. C. A.) 85 Fed. 508.

- "2. Or such a fraudulent transaction completed or contemplated by the acting managers, in connection with some other party, or among themselves, or with other shareholders as will result in serious injury to the corporation, or to the interests of the other shareholders;
- "3. Or where the board of directors, or a majority of them, are acting for their own interest, in a manner destructive of the corporation itself, or of the rights of the other shareholders;
- "4. Or where the majority of shareholders are oppressing and illegally pursuing a course in the name of the corporation, which is in violation of the rights of the other shareholders, and which can only be restrained by the aid of a court of equity.
- "5. Possibly other cases may arise in which, to prevent irremediable injury, or a total failure of justice, the court would be justified in exercising its powers, but the foregoing may be regarded as an outline of the principles which govern this class of cases.
- "6. But, in addition to the existence of grievances which call for this kind of relief, it is equally important that before the shareholder is permitted in his own name to institute and conduct a litigation which usually belongs to the corporation, he should show to the satisfaction of the court that he has exhausted all the means within his reach to obtain, within the corporation itself, the redress of his grievances, or action in conformity to his wishes. He must make an earnest, not a simulated effort, with the managing body of the corporation, to induce remedial action on their part, and this must be made apparent to the court. If time permits or has permitted, he must show, if he fails with the directors, that he has made an honest effort to obtain action by the stockholders as a body, in the matter of which he complains. And he must show a case, if this is not done, where it could not be done, or it was not reasonable to require it."394

paper Ass'n, 146 Mass. 495, 1 Cum. Cas. 769. 394 Hawes v. Oakland, 104 U. S. 450, 1 Smith's Cas. 282, 2 Keener's Cas. 1647, 1 Cum. Cas. 756.

In a Massachusetts case it was said by Judge Knowlton: "Courts of equity are swift to protect helpless minorities of stockholders of corporations from the oppression and fraud of majorities. But the legal relations into which the members of a corporation enter require them to seek redress for supposed wrongs done them as stockholders from its officers, and from the corporation itself, before applying elsewhere. Misconduct in dealing with a corporation, or in the management of its affairs, can affect its members only through the corporation it-The wrong in such a case is done primarily to the corporation. It is the duty of its directors or other managing officers to protect it from those who would do it injustice, and to seek compensation for any injury which it receives. holders in a corporation impliedly agree, when they join it, to act in the corporate business through officers chosen to represent them, and by vote at meetings of the members regularly called. And so, if they deem themselves aggrieved as shareholders by the dealings of others with it, by the acts of its managers, they are bound to seek their remedy through corporate channels, first, by application to the officers in charge, and, failing there, secondly, to the corporation itself, at a meeting of its members. If they can obtain justice at the hands of neither, the courts are open for their relief."395

### § 546. Defense by stockholders in suits against corporation.

When an action at law or suit in equity is brought against a corporation, it is for the corporation to defend, and the defense and management of the suit, like other matters relating to the affairs of the corporation, is within the discretion of the directors, and ordinarily stockholders cannot interfere except by electing a new board of directors. Except as hereafter stated, the stockholders cannot appear and answer or defend, either for the corporation or on their own behalf.396 It is immaterial that the stockholder owns all the stock of the corporation.<sup>397</sup>

<sup>295</sup> Dunphy v. Traveller Newspaper Ass'n, 146 Mass. 495, 1 Cum. Div. 13, 2 Keener's Cas. 1632, 1 Cum. Cas. 704; Park v. Ulster &

This does not apply, however, when suit is brought against a corporation by one who holds a majority of the stock, or otherwise controls the directors, and the suit is conducted fraudulently in his own interest, and against the interest of the corporation and the minority stockholders; or in any other case in which a corporation or its directors abuse their discretion in refusing to defend, or fail to prosecute the defense in good faith, and the stockholders cannot obtain relief within the corporation. In such cases, a stockholder, if the action is at law, may obtain relief by suing in equity, or if the suit is in equity, or under the code, a stockholder may intervene, and set up any defense which should properly be made by the corporation. 398

ley v. Pailthorp, 96 Mich. 287; Home Mining Co. v. McKibben, 60 Kan. 387.

A stockholder is not entitled to ask for a dismissal of an action against the corporation on the ground of the plaintiff's insolvency, and his assignee's refusal to continue the prosecution of the action. Hobbs v. Dane Mfg. Co., 5 Allen (Mass.) 581.

Where a corporation fails to interpose the statute of limitations as a bar against claims of creditors, individual stockholders cannot do so. Davis v. Gemmell, 73 Md. 530.

Laws of New York, 1892, c. 688, § 48, forbidding an insolvent corporation to suffer a judgment to be obtained with intent to prefer any particular creditor, does not allow a stockholder to apply to set aside such a judgment. In re Gardiner, 86 Hun (N. Y.) 30.

Kanawha Petroleum Co., 25 W. Va. stockholder to be summoned in, in 108; Park v. New York & Kanawha an action against an insolvent coroll Co., 26 W. Va. 486; Henry v. poration, and his personal liability Elder, 63 Ga. 347; Miller v. Murtorespond to the judgment recoveray, 17 Colo. 408; South-West Natural Gas Co. v. Fayette Fuel Gas viding that, if it should appear that Co., 145 Pa. St. 13; Farmers' Loan the stockholder was not liable, & Trust Co. v. Toledo, Ann Arbor & judgment should be entered in his N. M. Ry. Co., 67 Fed. 49; General favor, and at the same time judgment should be entered against the provement Co., 73 Fed. 386; Strad-corporation, a stockholder summoned in an action against the corporation could defend against personal liability only. He did not become a party to the action, so as to be entitled to defend the cause of action against the corporation, or remove the action from the superior to the supreme judicial court. Farnum v. Ballard Vale Machine Shop, 12 Cush. (Mass.) 507; Robbins v. Justices & Clerk of Superior Court, 12 Gray (Mass.) 225; Byers v. Franklin Coal Co., 14 Allen (Mass.) 470.

<sup>397</sup> Park v. Ulster & Kanawha Petroleum Co., 25 W. Va. 108.

398 Waymire v. San Francisco & San Mateo Ry. Co., 112 Cal. 646; Henry v. Traveler's Ins. Co., 16 Colo. 179; Morrill v. Little Falls Mfg. Co., 46 Minn. 260; Wilkinson v. Chemical Fire Ins. Co. of New Jersey, 2 N. Y. City Ct. Rep. 43; Bronson v. La Crosse & Milwaukee R. Co., 2 Wall. (U. S.) 283, 1 Under the Massachusetts statute Smith's Cas. 278; Farmers' Loan & of 1851 (chapter 315), allowing a Trust Co. v. Toledo, Ann Arbor &

Stockholders cannot dismiss an appeal by the corporation, or take an appeal for it from a judgment or decree against it.399

### Suit or defense by stockholder in the name of or for the corporation.

A stockholder, merely as such, has no authority, and is absolutely without the power, to file a bill or answer in the name of or for the corporation so as to make it a party. He cannot do so even by leave of court, for a corporation cannot be made a party in such a way. The only remedy of the stockholder, so as to bring the corporation before the court, is by a bill in equity, or cross-bill, in his own behalf, or in behalf of himself and other stockholders, making the corporation a party defendant, as explained in the preceding sections.400

#### Effect of assignment by corporation.

When a corporation makes a general assignment of all its

Taussig, 20 Colo. 44; Louisville & Oldham Turnpike Road Co. v. Ballard, 2 Metc. (Ky.) 165; State v. Holmes, 60 Neb. 40; Fitzwater v. National Bank of Seneca, 62 Kan. 163. Compare Meyer v. Bristol Hotel Co. (Mo.) 63 S. W. 96.

Where a stockholder intervened in a suit against the corporation, alleging that the suit was brought for the use of the president and two directors, who were a majority of the board, and the answer admitted the plaintiff's cause of action, it was held that the intervener was entitled to defend the suit without alleging a request to do so upon the officers. Schively v. Eureka Tellurium Gold Mining Co., 129 Cal. 293.

Under the Ohio statute (Rev. St. § 5114), which empowers the trial court, before or after judgment, in furtherance of justice, to amend any pleading, process, or proceeding, "by adding or striking out the name of any party," or "by inserting other allegations material to the cause," the court, after judg-

N. M. Ry. Co., 67 Fed. 49; Majors v. ment against a corporation, but at the same term, may in furtherance of justice permit a stockholder to intervene and answer to the merits. Henry v. Jeans, 48 Ohio St. 443.

In New York it is expressly provided that, if an action is brought against a corporation by procurement of its directors to enforce any claim to which it has a valid defense, and the corporation, by their connivance, makes default, any member may apply to the supreme court, on an affidavit stating such facts, for a stay of proceedings. Laws 1892, c. 687, § 28.

Under this provision, a stockholder showing such facts can have a default opened, and defend in behalf of the company. In re Virgil, 26 Misc. Rep. (N. Y.) 320.

300 Denver & Rio Grande Ry. Co. v. Alling, 99 U. S. 463; Ex parte Cutting, 94 U. S. 14; Silk Mfg. Co. v. Campbell, 27 N. J. Law, 539; Chicago & South Side Rapid Transit R. Co. v. Northern Trust Co., 90 Ill. App. 460.

400 Bronson v. La Crosse & Mil-

assets for the benefit of creditors, the assignee represents the corporation as well as its creditors, and unless he refuses to do so, he alone is authorized to bring a suit against the late directors of the corporation for negligence or mismanagement of its affairs, or to redress other injuries against, or enforce other rights of, the corporation. But if he wrongfully refuses to sue for redress, a stockholder may sue on behalf of himself and the other stockholders, as he could have done before the assignment if the corporation had refused to sue.401

#### § 549. Effect of dissolution of the corporation.

After a corporation has been dissolved by expiration of its charter, judgment of forfeiture, or otherwise, the stockholders are, in equity, entitled to its assets, in proportion to their stock, after payment of its debts, and as there is no longer any corporation, they may individually sue in equity to protect or enforce their rights, both as between themselves and as against third persons. 402 Persons who fraudulently represent that the entire stock of a corporation belongs to them, and thereby procure a dissolution of the corporation and possession of its assets, will be held as trustees ex maleficio at the suit of other stockholders. 403 The right of a stockholder to sue after dissolution of the corporation may not exist where there is a statutory provision continuing its existence for the purpose of suing and winding up its affairs, or vesting its assets in trustees for such purpose, with the power to maintain suits, etc. 404

waukee R. Co., 2 Wall. (U. S.) 283, Adm'r v. Shenandoah Valley R. Co., 1 Smith's Cas. 278; Cornell v. Sims, 28 W. Va. 623. See ante, § 328(b). 111 Ga. 828.

Bank, 89 Tenn. 630, 24 Am. St. Rep. 625. And see Williams v. Halliard, 38 N. J. Eq. 376; Ackerman v. Halsey, 37 N. J. Eq. 356; Jones v. Johnson, 86 Ky. 530; Savings Bank of Louisville's Assignee v. Carpenter, 87 Ky. 306, 12 Am. St. Rep. 488; Brinckerhoff v. Bostwick, 88 N. Y. 52.

402 Putnam v. Ruch, 54 Fed. 216, 56 Fed. 416; Chouteau v. Allen, 70 Mo. 290. And see Crumlish's

28 W. Va. 623. See ante, § 328(b). A stockholder of a dissolved cor-401-Wallace v. Lincoln Savings poration has such an interest as Bank, 89 Tenn. 630, 24 Am. St. Rep. entitles him to sue, under Code La. art. 606, to annul a judgment against the corporation, which is void because rendered after its dissolution, where he is individually liable under the charter for the debts of the corporation to the extent of his shares. Musson v.

Richardson, 11 Rob. (La.) 37. 403 Bailey's Appeal, 96 Pa. St.

404 Taylor v. Holmes, 127 U.S.

#### § 550. Suits by stockholders in the federal courts.

It is now well settled that, where the necessary diversity of citizenship exists, the federal courts have jurisdiction of a suit by a stockholder, on behalf of himself and other stockholders, to prevent or redress injuries to the corporation.405 But the right to maintain such a suit is regulated by Equity Rule 94. adopted by the supreme court of the United States for the purpose of guarding against collusion of parties for the purpose of bringing cases within the jurisdiction of such courts. This rule is as follows: "Every bill brought by one or more stockholders in a corporation, against the corporation and other parties, founded on rights which may properly be asserted by the corporation, must be verified by oath, and must contain an allegation that the plaintiff was a shareholder at the time of the transaction of which he complains, or that his share had devolved on him since by operation of law; and that the suit is not a collusive one to confer on a court of the United States jurisdiction of a case of which it would not otherwise have cognizance. It must also set forth with particularity the efforts of the plaintiff to secure such action as he desires on the part of the managing

489; General Electric Co. v. West Asheville Improvement Co., 73 Fed. 386; ante, § 331 et seq.

<sup>405</sup> Dodge v. Woolsey, 18 How. (U. S.) 331, 1 Smith's Cas. 257, 2 Keener's Cas. 1605, 1 Cum. Cas. 739; Greenwood v. Union Freight R. Co., 105 U. S. 13, 2 Smith's Cas. 720, 1 Keener's Cas. 192; Pond v. Vermont Valley R. Co., 12 Blatchf. 280, Fed. Cas. No. 11,265; Barnes v. Kornegay, 62 Fed. 671.

In order that the federal courts may have jurisdiction, the plaintiff and the defendants must be citizens of different states. If the plaintiff and some of the defendants, or some of the plaintiffs and some of the defendants, are citizens of the same state, there is no jurisdiction. Central Railroad feated by other stockholders com-S. 249; East Tennessee, Virginia & ham, 115 U.S. 61.

G. R. Co. v. Grayson, 119 U. S. 240; Leary v. Columbia River & Puget Sound Navigation Co., 82 Fed. 775; Bell v. Donohoe, 17 Fed. 710; Wilder v. Virginia T. & C. Steel & Iron Co., 46 Fed. 676. An Quincy v. Steel, 120 U. S. 241. And see

The plaintiff cannot give the court jurisdiction by omitting a necessary party defendant who is a citizen of the same state. Wilder v. Virginia, T. & C. Steel & Iron Co., 46 Fed. 676; Douglas v. Richmond & Danville R. Co., 106 N. C.

But he is not bound to make a stockholder a party plaintiff if it will defeat the jurisdiction. Pond v. Vermont Valley R. Co., 12 Blatchf. 280, Fed. Cas. No. 11,265.

Co. of New Jersey v. Mills, 113 U. ing in as plaintiffs. Stewart v. Dun-

directors or trustees, and, if necessary, of the shareholders, and the causes of his failure to obtain such action."

Under this rule a bill is demurrable if it fails to allege that the plaintiff was a shareholder at the time of the transaction of which he complains, or that his share has since devolved upon him by operation of law; and that the suit is not a collusive one to confer on a court of the United States jurisdiction in a case of which it would otherwise have no cognizance.406 demurrable if it fails to show with particularity, as required by the rule, efforts on the part of the plaintiff to secure action by the directors or trustees, or the shareholders, and the causes of his failure to obtain such action, so as to show a right to sue. 407 It is not necessary, however, that it shall show a request upon the directors or other shareholders to sue or take other action, if it shows that they are the parties guilty of the wrongs complained of, or that, for any other reason, such a request would have been useless; but it must particularly set forth the facts excusing failure to make such a request.408

110 U. S. 209, 1 Cum. Cas. 765: Louisiana Electric Light Co., 68 Fed. 673; Taylor v. Holmes, 127 U.

er may sue to enjoin a misapplication of corporate funds under Fed. 176; De Neufville v. New York an agreement entered into before his stock was issued, if he had a Fed. 10; Hutton v. Joseph Banvested right to receive the stock before the agreement was made. Hill v. Glasgow R. Co., 41 Fed.

407 Dodge v. Woolsey, 18 How. (U. S.) 331, 1 Smith's Cas. 257, 2 Keener's Cas. 1605, 1 Cum. Cas. 739; Memphis City v. Dean, 8 Wall. (U. S.) 64; Dannmeyer v. Coleman, 11 Fed. 97; Taylor v. Holmes, 14 Fed. 498, 127 U. S. 489; Putnam v. Ruch, 54 Fed. 216, 56 Fed. 416; Whitney v. Fairbanks, 54 Fed. 985;

406 Hawes v. Oakland, 104 U. S. Bill v. Western Union Telegraph 450, 1 Smith's Cas. 282, 2 Keener's Co., 16 Fed. 14; Foote v. Cunard Cas. 1647, 1 Cum. Cas. 756; Drinp-Mining Co., 17 Fed. 46; McHenry fell v. Ohio & Mississippi Ry. Co., v. New York, Pennsylvania & O. R. Co., 22 Fed. 130; Squair v. Lookout United Electric Securities Co. v. Mountain Co., 42 Fed. 729; Weidenfeld v. Allegheny & K. R. Co., 47 Fed. 11; Swope v. Villard, 61 Fed. Fed. 613; Asylor V. Holmes, 121 U. Fed. 11, Swope V. Vinlard, U. Fed. 88, 489; Dannmeyer v. Coleman, 11 417; Holton v. Wallace (C. C. A.) Fed. 97; Robinson v. West Virginia 77 Fed. 61; Church v. Citizens' Loan Co., 90 Fed. 770. Street R. Co., 78 Fed. 526; Ziegler It has been held that a stockhold- v. Lake Street Elevated R. Co. (C. C. A.) 76 Fed. 662, affirming 69 & Northern Ry. Co. (C. C. A.) 81 croft & Sons Co., 83 Fed. 17; Clarke v. Eastern Building & Loan Ass'n, 89 Fed. 779; Edwards v. Bay State Gas Co., 91 Fed. 942; Robinson v. West Virginia Loan Co., 90 Fed. 770; Ball v. Rutland R. Co., 93 Fed. 513. Compare Old Colony Trust Co. v. Dubuque Light & Traction Co., 89 Fed. 794.

See the above cases as to the sufficiency of a bill in this respect. 408 Excelsior Pebble Phosphate Co. v. Brown, 42 U. S. App. 55, 74

### \$ 551. Persons entitled to sue as stockholders.

In order that a person may maintain a suit as a stockholder to set aside or enjoin an ultra vires transaction, or to redress or prevent other injuries to the corporation, he must be a stockholder in fact when the suit is brought. If he has not yet become a stockholder by reason of nonperformance of his contract of subscription or contract for the purchase of shares, or by reason of the fact that his subscription is upon a condition precedent which has not yet been performed by the corporation, or if he has ceased to be a stockholder by reason of a transfer or forfeiture of his shares, he has no standing to complain.409 It has been held that a mere equitable right to shares is not enough to give one a standing to sue;410 but since the suit is in equity, there is no reason why an equitable right cannot be protected, as well as a legal right. 411 If the plaintiff is in fact a bona fide stockholder, however, it is immaterial how he became such, or whether or not he became such on a bona fide subscription for The holder of watered stock may maintain such a suit, when the stock is valid as between him and the corporation;413 but it is otherwise where his certificate is an absolute nullity because of an express statutory or constitutional prohibition.414

No. 11,265; Sellers v. Phoenix Iron Co., 13 Fed. 20; Earle v. Seattle, C. A.) 89 Fed. 783.

Lake Shore & E. Ry. Co., 56 Fed. 909; Young v. Alhambra Mining Co., 71 Fed. 810; County of Tazewell v. Farmers' Loan & Trust Co., 12 Fed. 752; Rogers v. Nashville, Hun (N. Y.) 248; Fitchett v. Murchattanooga & St. L. Ry. Co. (C. A.) 91 Fed. 299; Ball v. Rutland R. Co., 93 Fed. 513; Eldred v. American Palace-Car Co., 99 Fed. 168; Berwind v. Canadian Pacific Ry. Co., 98 Fed. 158.

As to the sufficiency of a stock-side of the sufficiency of the sufficiency of a stock-side of the sufficiency of the sufficie

As to the sufficiency of a stockholder's bill in this respect, see the cases above cited.

No demand by a stockholder on the officers of the corporation to bring suit against another stockholder is necessary under equity rule 94, before suing in his own name, when 64. And see ante, § 395(b).

Fed. 321; Pond v. Vermont Valley the right of action is one which R. Co., 12 Blatchf. 280, Fed. Cas. the corporation could not enforce No. 11,265; Sellers v. Phoenix Iron in its entirety. Barcus v. Gates (C.

411 See Great Western Ry. Co. v. Rushout, 5 De Gex & S. 290; Fisher v. Patton, 134 Mo. 32.

412 Stewart v. Erie & Western Transp. Co., 17 Minn. 372.

413 See ante, § 395 (a).

414 Hinckley v. Pfister, 83 Wis.

The fact that a stockholder suing to enjoin or obtain redress from another corporation also holds stock in the latter corporation does not preclude him from maintaining the suit.415

Such a suit may be brought by an administrator or executor having the title to shares as such, or by any person holding shares in trust; 416 or by a cestui que trust of shares, if the trustee refuses to sue, and is made a party defendant,417 or by a pledgee of shares,418 or by the pledgor.419

A stockholder cannot sue in equity in the federal courts to set aside or enjoin an ultra vires transaction, or redress a misapplication of corporate assets, or to enjoin or obtain redress for fraud or negligence on the part of the directors or other shareholders, etc., unless he was a stockholder at the time of the transactions complained of, or his shares have devolved upon him since by operation of law; 420 and the same rule has been asserted in Georgia upon the authority of the decisions of the supreme court of the United States. 421 The decisions and dicta in the federal courts, however, are not based upon any general principle, but upon an equity rule adopted by the supreme court, 422 and which was designed as a rule of practice merely, to guard those courts against collusion of parties for the purpose of bringing cases within their jurisdiction; 423 and they are no authority whatever as applied to suits in the state courts. By the weight of authority, in the absence of such a rule, a stockholder is not precluded from suing in equity on behalf of himself and other stockholders by the mere fact that he purchased his shares after the transactions complained of, even though he may have known of them at the time of his purchase, and though

<sup>416</sup> Scanlan v. Snow, 2 App. D. C. 137; Jones v. Pearl Mining Co., 20 Colo. 417.

<sup>417</sup> Great Western Ry. Co. v. 536, 12 Am. St. Rep. 337. Rushout, 5 De Gex & S. 290.

<sup>418</sup> Campbell v. American Zylonite Co., 122 N. Y. 455; Chafee v. Parsons v. Joseph, 92 Ala. 403, 1 Quidnick Co., 14 R. I. 75; Baldwin Smith's Cas. 311, 2 Keener's Cas. v. Canfield, 26 Minn. 43; Green v. 1653.

<sup>415</sup> Carter v. Producers & Re-Hedenberg, 159 Ill. 489, 50 Am. St. finers Oil Co., 164 Pa. St. 463. Rep. 178; post, § 622.

<sup>419</sup> Fisher v. Patton, 134 Mo. 32.

<sup>420</sup> Post, § 550.

<sup>421</sup> Alexander v. Searcy, 81 Ga.

<sup>422</sup> See post, § 550.

<sup>423 1</sup> Morawetz, Priv. Corp. § 269;

he may have made the purchase for the purpose of acquiring a standing to sue, for the transfer of stock not only conveys to the transferee the ownership of the shares and the right to the future dividends thereon, but also places him upon an equal footing with the other stockholders-provided neither he nor his transferrer is otherwise estopped—in respect to the right to call the officers and agents of the corporation to account, and to enjoin or set aside ultra vires transactions, etc. 424 And ordinarily the motive in acquiring the shares and bringing suit is immaterial.425

It is clear, however, that a person who purchases shares in a corporation with knowledge of the fact that his transferrer is estopped, by laches, participation, or acquiescence, to complain of a previous ultra vires transaction or misapplication of funds, is in precisely the same position as his transferrer, and is also estopped. 426 And it is also established by the weight of authority that a transferee of shares is in the same position as his transferrer with respect to suing on account of transactions prior to the transfer, even when he is a purchaser without notice; and that he is estopped to sue, therefore, without regard to his good faith, if his transferrer was estopped.427 This doctrine, of

424 Seaton v. Grant, 2 Ch. App. incomplete transfer of the prop-459, 1 Smith's Cas. 307; Bloxam v. erty of the corporation may be en-Metropolitan Ry. Co., 3 Ch. App. joined at the suit of stockholders 337; Winsor v. Bailey, 55 N. H. 218, who acquired their stock after the Joseph, 92 Ala. 405, 1 Sintis Cas. V. Botton & Montana Constitution 311, 2 Keener's Cas. 1653; Carson Copper & Silver Mining Co., 21 v. Iowa City Gaslight Co., 80 Iowa Mont. 544. 638; City of Chicago v. Cameron, 425 Post, § 552. 22 Ill. App. 91, 120 Ill. 447; Elkins v. Camden & Atlantic R. Co., 36 N. J. Eq. 5, 1 Keener's Cas. 722; Pender v. Lushington, 6 Ch. Div. 70; Ervin v. Oregon Railway & Navigation Co., 28 Hun (N. Y.) 269; Ramsey v. Gould, 57 Barb. (N. Y.) 398; Frothingham v. Broadway & Seventh Avenue R. Co., 9 N. Y. Civ. Proc. Rep. 304. Compare Clark v. American Coal

Co., 86 Iowa, 436.

The ratification by a majority of the stockholders of an illegal and

Parsons v. transfer was attempted. Forrester 1 Smith's Cas. 310; Parsons v. transfer was attempted. Forrester Joseph, 92 Ala. 403, 1 Smith's Cas. v. Boston & Montana Consolidated

426 Ffooks v. South Western Ry. Co., 1 Smale & G. 142; Parsons v. Joseph, 92 Ala. 403, 1 Smith's Cas. 311, 2 Keener's Cas. 1653; In re Syracuse, Chenango & N. Y. R. Co., 91 N. Y. 1.

427 Parsons v. Hayes, 14 Abb. N. C. (N. Y.) 419, 1 Smith's Cas. 314; Da Ponte v. Louisiana State Lottery Co., 1 La. Law J. 184, Fed. Cas. No. 3,569; Clark v. American Coal Co., 86 Iowa, 436.

Contra. Parsons v. Joseph, 92

course, does not preclude a transferee of shares from enjoining ultra vires acts subsequent to the transfer. It can never be held, said Lord Chancellor Chelmsford in an English case, that the acquiescence of the original holder of stock in illegal acts of the quectors of the corporation will bind a subsequent holder of that stock to submit to all future acts of the same character. 428

A person cannot sue as a stockholder unless he is the bona fide owner of the stock upon which his right to sue is based. He cannot sue if the transfer to him was merely nominal, and not in good faith, but merely for vexatious purposes. 429 have seen, however, a stockholder is not precluded from suing by the mere fact that he purchased his shares for the purpose of suing.

A stockholder is not precluded from suing as such by the fact that the transfer of the stock to him is not registered on the books of the corporation, particularly where he has applied to have it registered and the corporation has refused.430

#### Motive of stockholder in suing—Extent of interest. § 552.

It is a general rule that, if a stockholder comes into a court of equity in the bona fide character of a stockholder to enjoin or set aside ultra vires transactions on the part of the directors or a majority of the stockholders, or to obtain other relief for injuries to the corporation, and shows a right to relief, the court cannot properly inquire into his motive in prosecuting the suit.431 It was said by Lord Chancellor Westbury in an English

er's Cas. 1653.

428 Bloxam v. Metropolitan Ry. Co., 3 Ch. App. 337.

429 Moore v. Silver Valley Mining Co., 104 N. C. 534; McDonnell v. Grand Canal Co., 3 Ir. Ch. 578.

430 Great Western Ry. Co. v. Rushout, 5 De Gex & S. 290; Bagshaw v. Eastern Union Ry. Co., 7 2 Keener's Cas. 446, 1 Cum. Cas. Hare, 114; Parrott v. Byers, 40 Cal. 136; Central R. Co. v. Collins, 40 614; Carson v. Iowa City Gaslight Ga. 582, 1 Keener's Cas. 706; El-Co., 80 Iowa, 638; Ervin v. Oregon kins v. Camden & Atlantic R. Co., Co., Co., 20 Iowa, 638; Ervin v. Oregon kins v. Camden & Cas. 702; Cas. 722; Cas. Railway & Navigation Co., 28 Hun 36 N. J. Eq. 5, 1 Keener's Cas. 722;

Ala. 403, 1 Smith's Cas. 311, 2 Keen- (N. Y.) 269; Baldwin v. Canfield, 26 Minn. 43.

431 Forrest v. Manchester, Sheffield & L. Ry. Co., 4 De Gex, F. &. J. 126, 1 Smith's Cas. 304, 2 Keener's Cas. 1600, 1 Cum. Cas. 713; Seaton v. Grant, 2 Ch. App. 459, 1 Smith's Cas. 307; Colman v. Eastern Counties Ry. Co., 10 Beav. 1,

case: "I have nothing to do with the motives of plaintiffs suing in this court. If they come here in a bona fide character, the reason for their coming here is a matter beyond the province of a court of justice to inquire into."432

According to the weight of authority, however, a stockholder must sue in good faith as such, and for the company, and not as the mere puppet of, and for the interest of, a rival company. By the weight of authority, therefore, although there seem to be some decisions or dicta to the contrary, a suit by a stockholder on behalf of himself and other stockholders should be dismissed if it appears that he does not sue in good faith in the interest of the other stockholders, or in his own interest as a stockholder. but solely in the interest of a rival corporation, in which he is also a stockholder, by its direction, and under an agreement by it to indemnify him for costs.433

Ramsey v. Gould, 57 Barb. (N. Y.) 398; Lewisohn Bros. v. Anaconda Copper Mining Co., 26 Misc. Rep. (N. Y.) 613, 623.
Compare, however, Sparhawk v.

Union Passenger Ry. Co., 54 Pa. St. 401; Clark v. American Coal Co., 86 Iowa, 436.

432 Forrest v. Manchester, Sheffield & L. Ry. Co., 4 De Gex, F. & J. 126, 1 Smith's Cas. 304, 2 Keen-

er's Cas. 1600, 1 Cum. Cas. 713. 488 Forrest v. Manchester, Sheffield & L. Ry. Co., 4 De Gex, F. & J. 126, 1 Smith's Cas. 304, 2 Keener's Cas. 1600, 1 Cum. Cas. 713. In this case the directors of the rival corporation directed the institution of the suit, and indemnified the plaintiff against costs. Lord Chancellor Westbury said: "It has been a very wholesome doctrine of this court that one shareholder having in view the legitimate purposes of the company may be permitted in this court to maintain a suit on

putably requires that the suit shall be a bona fide one, faithfully, truthfully, sincerely directed to the benefit and the interests of those shareholders whom the plaintiff claims a right to represent. But can I permit a man who is the puppet of another company to represent the shareholders of the against whom he desires to establish the interests and benefits of a rival scheme? That would be entirely contrary to the principle upon which this constructive representation has been permitted to be founded. When the plaintiff sues in that capacity any personal exception to the plaintiff remains, and it would be in direct contradiction of every principle of truth and justice if I permitted a man to come here clothed in the garb of a shareholder of company A., but who is in reality a shareholder in company B., and has no sympathy whatever with, no real purpose of behalf of himself and the other promoting the interests of the shareholders of the company, but other company. Such a thing the principle upon which that con-would be so much at variance with structive representation of the the principles of a court of equity shareholders is permitted indisthat it would be impossible for it

As we have seen in a former section, the fact that the plaintiff purchased his stock for the purpose of bringing suit does not preclude him.434

When a stockholder sues to enjoin the directors of a corporation from applying its assets to purposes not authorized by its charter or to prevent or redress other wrongs, his right to relief is not in any way affected by the fact that he holds little stock in the corporation, so that his share (in equity) of the amount which it is proposed to misapply, or the extent of his injury, is comparatively trivial. Notwithstanding this, he has the same right as the largest stockholder to insist that the assets of the corporation shall not be diverted from the objects for which it was created. The maxim, De minimis non curat lex, does not apply.435

# § 553. Laches and estoppel of stockholders.

Even when a stockholder would otherwise be entitled to maintain a suit in equity under the principles stated in the preceding

to entertain a suit of that descrip- Bros. v. Anaconda Copper Mining tion which is a mere mockery, a Co., 26 Misc. Rep. (N. Y.) 613, 623. mere illusory proceeding." And see to the same effect, Waterbury v. Merchants' Union Express Co., 50 to dissolve a corporation was filed

1, 2 Keener's Cas. 446, 1 Cum. Cas. 136. Central R. Co. v. Collins, 40 object was to dissipate rather than Ga. 582, 1 Keener's Cas. 706, and to dissolve the assets, it was held Sandford v. Catawissa, Williamsport & E. R. Co., 24 Pa. St. 378, 64 Am. Dec. 667, which are apparently to the contrary.

suit by a stockholder to restrain the company from leasing its property, was dissolved, where it apsuing in good faith for the protection of his own rights, but at the instigation and in the interest of 13 Grant Ch. (Can.) 552; Kean v. a rival corporation. Jenkins v. Johnson, 9 N. J. Eq. 401; Gifford Auburn City Ry. Co., 27 App. Div. v. New Jersey R. & Transp. Co., (N. Y.) 553. Compare Lewisohn 10 N. J. Eq. 171; Elkins v. Cam-

In an Illinois case, where it appeared that a bill by a stockholder Barb. (N. Y.) 157; Beshoar v. in pursuance of an agreement with Chappell, 6 Colo. App. 323. the officers of other corporations Compare, however, Colman v. against which the corporation Eastern Counties Ry. Co., 10 Beav. sought to be dissolved had an important suit pending, and that the that the bill should be dismissed. Watson v. Le Grand Roller Skating Rink Co., 177 Ill. 203.

434 Ante, § 554, note 424. In a New York case, an injunction pendente lite, granted in a Ry. Co., 35 Ch. Div. 675, 1 Smith's Cas. 300; Seaton v. Grant, 2 Ch. App. 459, 1 Smith's Cas. 307; Beman v. Rufford, 1 Sim. (N. S.) 550; peared that the plaintiff was not Charlton v. Newcastle & Carlisle Ry. Co., 5 Jur. (N. S.) 1096; Armstrong v. Toronto Church Society,

sections, his right to relief may be barred by laches, or he may be estopped to complain by reason of acquiescence, consent, or participation in the acts complained of.

(a) Laches.—If a stockholder, with knowledge of wrongful acts on the part of the directors or a majority of the stockholders, stands by for an unreasonable time without taking any steps to set the same aside, and rights are acquired by others, his right to maintain a suit to set the transaction aside is barred by his laches, however clear his right to relief would have been if he had moved promptly.436 The general rule is "that while a minority of the stockholders of a corporation may maintain a bill in equity in behalf of themselves and other stockholders, for fraud, conspiracy, or acts ultra vires, against a corporation, its officers and others who participate therein, when the minority stockholders have been injured or damaged by said acts, they

briskie v. Cleveland, Columbus & C. R. Co., 23 How. (U. S.) 381.
Compare Greenough v. Alabama Great Southern R. Co., 64 Fed. 22; Dannmeyer v. Coleman, 11 Fed. 97; Benedict v. Western Union Tele-graph Co., 9 Abb. N. C. (N. Y.) 214.

486 England: Houldsworth v. Evans, L. R. 3 H. L. 263; Gregory v. Patchett, 33 Beav. 595.

States: Drimpfell United Ohio & Mississippi Ry. Co., 110 U. S. 209, 1 Cum. Cas. 765; Allen v. Wilson, 28 Fed. 677; Taylor v. South & North Alabama R. Co., 4 Woods, 575, 13 Fed. 152; Pacific R. Co. v. Missouri Pacific Ry. Co., 12 Fed. 641; Hazard v. Credit Mobilier of America, 38 Fed. 195. California: Wills v. Porter (Cal.)

California: 61 Pac. 1109.

Connecticut: Banks v. Judah, 8 Conn. 145.

Alexander v. Searcy, 81 Ga. 536, 12 Am. St. Rep. 337.

Illinois: Levin v. Chicago Gas Light & Coke Co., 64 Ill. App. 393. Iowa: Thompson v. Lambert, 44 Iowa, 239.

Massachusetts: Peabody v. Flint, 9 Bush (Ky.) 468.

den & Atlantic R. Co., 36 N. J. 6 Allen, 54, 1 Smith's Cas. 263, 1 Eq. 5, 1 Keener's Cas. 722; Zabriskie v. Cleveland, Columbus & eller Newspaper Ass'n, 146 Mass. C. R. Co., 23 How. (U. S.) 381. 495, 1 Cum. Cas. 769.

Minnesota: Stewart v. Erie & Western Transp. Co., 17 Minn. 372. New Jersey: Rabe v. Dunlap, 51 N. J. Eq. 40.

New York: Hoyt v. Quicksilver Mining Co., 17 Hun, 169; Warren v. Bigelow Blue Stone Co., 74 Hun, 304; Roberts v. New York & New England R. Co., 31 N. Y. Supp. 577; Marbury v. Stone, 17 App. Div. 352, affirmed 160 N. Y. 701.

Pennsylvania: Ashurst's peal, 60 Pa. St. 290; Watts' Appeal, 78 Pa. St. 370; Fredericks v. Pennsylvania Canal Co., 109 Pa. St. 50.

Rhode Island: Boston & Providence R. Corp. v. New York & New England R. Co., 13 R. I. 260; Emerson v. New York & New England R. Co., 14 R. I. 555.

Tennessee: Cullen v. Coal Creek Mining & Mfg. Co. (Tenn. Ch. App.) 42 S. W. 693.

West Virginia: Boyce v. Montauk Gas Coal Co., 37 W. Va. 73.

Compare, however, Covington & Lexington R. Co. v. Bowler's Heirs, must act promptly, and not wait an unreasonable length of time. If they postpone their complaint for an unreasonable time, they forfeit their right to equitable relief. Nothing will call a court of equity into activity but conscience, good faith, and reasonable diligence. When these are wanting, the court is passive and does nothing."437

This is not on the ground that the laches or acquiescence of the stockholder renders the transaction legal, but on the ground that, by reason of his laches, he is without equity. "His acquiescence does not render valid the illegal act of the corporation, but will prevent him from taking advantage of its invalidity."438

If a stockholder acts as soon as he learns of a fraudulent or illegal transaction, and takes all reasonable steps to obtain relief within the corporation, and, as soon as he finds that he is unable to do so, brings suit to set the transaction aside, he is not chargeable with laches. 439 And stockholders are not chargeable with laches because they remain still while some of their number are seeking to impeach the transaction.440

(b) Estoppel by consent, acquiescence, or participation.-A stockholder who participates as an officer or as a stockholder in illegal or ultra vires transactions on the part of the directors or stockholders, or consents thereto, or who, with full knowledge of the intention to engage in such transactions, acquiesces therein, instead of objecting and taking steps to prevent the same, is estopped to afterwards sue in equity to set the transactions aside; and it can make no difference that he sues on behalf of himself and other stockholders, and that there are other stock-

<sup>536, 12</sup> Am. St. Rep. 337.

<sup>536, 12</sup> Am. St. Rep. 337.

<sup>&</sup>amp; Iron Co. v. Sherman, 30 Barb. (N. Y.) 553; Hoffman Steam Coal

Minority stockholders are not Y.) 103.

<sup>437</sup> Alexander v. Searcy, 81 Ga. guilty of laches in waiting until 6, 12 Am. St. Rep. 337. the day before the time set for 6, 12 Am. St. Rep. 337. the day before the time set for 438 Alexander v. Searcy, 81 Ga. ratification by the majority of an illegal and incomplete transfer of 439 Byrne v. Schuyler Electric the corporate property before suing Mfg. Co., 65 Conn. 336. See, also, for an injunction. Forrester v. Gilman, Clinton & S. R. Co. v. Boston & Montana Consolidated Kelly, 77 Ill. 426; Cumberland Coal Copper & Silver Mining Co., 21 Mont. 544.

<sup>440</sup> Metropolitan Elevated Ry. Co. Co. v. Cumberland Coal & Iron Co., v. Manhattan Elevated Ry. Co., 11 16 Md. 456, 77 Am. Dec. 311. Daly (N. Y.) 373, 14 Abb. N. C. (N.

holders who might maintain the suit.<sup>441</sup> The same is true where a stockholder expressly or by his conduct subsequently ratifies the transaction.<sup>442</sup> Mere silence of a stockholder when others state their purpose to use the funds of the corporation for an unauthorized purpose is not equivalent to participation or

441 England: Burt v. British Nation Life Assurance Ass'n, 4 De Gex & J. 158, 1 Smith's Cas. 293.

United States: Dimpfell v. Ohio & Mississippi Ry. Co., 110 U. S. 209, 1 Cum. Cas. 765; Allen v. Wilson, 28 Fed. 677; McGeorge v. Big Stone Gap Improvement Co., 57 Fed. 262; Barr v. Pittsburgh Plate Glass Co., 51 Fed. 33; Holton v. Wallace, 66 Fed. 409; Post v. Beacon Vacuum Pump & Electrical Co. (C. C. A.) 84 Fed. 371.

Alabama: Memphis & Charleston R. Co. v. Grayson, 88 Ala. 572, 16 Am. St. Rep. 69; Parsons v. Joseph, 92 Ala. 403, 1 Smith's Cas. 311, 2 Keener's Cas. 1653.

Connecticut: Terry v. Eagle Lock Co., 47 Conn. 141.

Georgia: Cozart v. Georgia Railroad & Banking Co., 54 Ga. 379; Memphis Branch R. Co. v. Sullivan, 57 Ga. 240.

Illinois: Perry v. Pearson, 135 Ill. 218.

Iowa: Thompson v. Lambert, 44 Iowa, 239; Hart v. Mt. Pleasant Park Stock Co., 97 Iowa, 353.

Kentucky: Browning v. Mullins (Ky.) 13 S. W. 427.

Maine: Belknap v. Davis, 19 Me. 455.

Massachusetts: Dunphy v. Traveller Newspaper Ass'n, 146 Mass. 495, 1 Cum. Cas. 769.

Nebraska: Clarke v. Omaha & Southwestern R. Co., 4 Neb. 458.

New Jersey: Zabriskie v. Hackensack & New York R. Co., 18 N. J. Eq. 178, 90 Am. Dec. 617, 2 Smith's Cas. 760, 2 Keener's Cas, 1487, 1 Cum. Cas. 781; Trimble v. American Sugar-Refining Co. (N. J.) 48 Atl. 912; Rabe v. Dunlap, 51 N. J. Eq. 40.

New York: Parsons v. Hayes, Ky. Law Rep. 431.

14 Abb. N. C. (N. Y.) 419, 1 Smith's Cas. 314; McNab v. McNab & Harlin Mfg. Co., 62 Hun, 18, 1 Smith's Cas. 332, affirmed on the opinion below in 133 N. Y. 687; Burden v. Burden, 159 N. Y. 287, affirming 8 App. Div. 160; Barr v. New York, Lake Erie & W. R. Co., 125 N. Y. 263.

Pennsylvania: Coleman v. Columbia Oil Co., 51 Pa. St. 74; Watt's Appeal, 78 Pa. St. 370; Fredericks v. Pennsylvania Canal Co., 109 Pa. St. 50; Clark v. Pittsburg Natural Gas Co., 184 Pa. St. 188.

Washington: Roy & Co. v. Scott, Hartley & Co., 11 Wash. 399.

The bill must negative acquiescence. Trimble v. American Sugar-Refining Co. (N. J. Ch.) 48 Atl. 912.

A stockholder in a corporation who has agreed to and assisted in an arrangement whereby the corporation became possessed of certain property cannot afterwards question its power to hold the same. Burden v. Burden, 159 N. Y. 287, affirming 8 App. Div. 160.

The acquiescence of a stockholder will not estop him to sue for the benefit of the corporation for wrongs committed by the managing officers against it for the benefit of another corporation of which they were also officers. Fitzgerald v. Fitzgerald & Mallory Construction Co., 41 Neb. 374, 429.

442 Cozart v. Georgia Railroad & Banking Co., 54 Ga. 379; Berry v. Broach, 65 Miss. 450; Fredericks v. Pennsylvania Canal Co., 109 Pa. St. 50; Coleman v. Columbia Oil Co., 51 Pa. St. 74; Maxville, W. & L. Turnpike Road Co. v. Barnes, 14 Ky. Law Rep. 431.

acquiescence, and does not estop him to object and sue to enjoin the misapplication.443

This doctrine prevents a stockholder who has participated as an officer or stockholder in making an ultra vires lease or other continuing contract, or in engaging in an ultra vires business, from afterwards suing in equity to set the lease or contract aside, or to enjoin the corporation from continuing such business. would be manifestly inequitable to the corporate entity, and to other stockholders, said the Alabama court in such a case, to allow a stockholder, so long as the course in which he has set the company continues to be the corporate policy, to appeal to the courts to have that policy reversed, and the company coerced into a different line of conduct.444 Where a corporation organized for the purpose of manufacturing and selling brass and iron goods had for a long time engaged with profit in buying iron pipes to sell with the goods manufactured by it, in order to complete the orders received from customers, it was held that a stockholder who made no objection to such departure from its objects, and who accepted part of the profits as dividends, was precluded from maintaining any proceeding against the officers on the ground that the dealing in iron pipes was ultra vires.445 It has been held, however, that a stockholder is not precluded from objecting and suing to enjoin an ultra vires transaction because he has consented to or acquiesced in former transactions of a similar character.446

It has been held that, if a contract is illegal and void, as being in violation of an express prohibition, or contrary to public

<sup>489, 50</sup> Am. St. Rep. 178.

v. Grayson, 88 Ala. 572, 16 Am. St.

corporation doing a similar busisix years, without objection from Pa. St. 379; Coquard National Linthe minority stockholders, does not seed Oil Co., 171 Ill. 480.

<sup>443</sup> Green v. Hedenberg, 159 Ill. estop the latter from restraining such control in the future. George 444 Memphis & Charleston R. Co. v. Central Railroad & Banking Co., 101 Ala. 607.

Rep. 69.

It has been held, however, that the fact that a corporation owning a majority of the stock of another opinion below in 133 N. Y. 687.

<sup>446</sup> Bloxam v. Metropolitan Ry. ness in the same field has illegally Co., 3 Ch. App. 337. See, also, exercised control of the latter for Manderson v. Commercial Bank, 28

policy, and not merely ultra vires, the fact that a stockholder voted therefor as a director or otherwise consented or participated does not estop him from attacking its validity.447 weight of authority, however, is to the contrary 448

#### § 554. Parties to suits by stockholders.

When a stockholder sues in equity to enforce a right belonging to the corporation, or to enjoin or redress an injury to the corporation, all the stockholders are interested in the result of the suit. It is not for his own benefit alone, but for the benefit of all the stockholders, and it must therefore be brought on behalf of the complainant, and all other stockholders other than such, if any, as are made defendants.449 Other stockholders may come into such a suit to take the benefit of the proceedings and decree, not to oppose and nullify them. 450 A single stockholder may sue on his own behalf alone to enjoin a corporation from commencing or continuing an ultra vires act, or misapplying its funds, 451

447 Bostwick v. Chapman, 448 Stewart v. Erie & Western Transp. Co., 17 Minn. 372, where it was held that a stockholder who consented to a contract creating a

monopoly could not afterwards sue to set it aside. His rights, it was said, are determined upon the same principles as in cases where the contract is merely ultra vires. See, also, Gray v. Chaplin, 2 Russ. 126; Manderson v. Bank, 28 Pa. St. 379. Manderson v. Commercial

449 Taylor v. Salmon, 4 Mylne & C. 134; Jefferson County Savings Bank v. Francis, 115 Ala. 317; March v. Eastern R. Co., 40 N. H. 548, 77 Am. Dec. 732; Wickersham v. Crittenden, 93 Cal. 17; McAfee v. Zettler, 103 Ga. 579. It has been held, however, that

a suit in which the plaintiff prays

a party plaintiff on application. Wood v. Union Gospel Church Building Ass'n, 63 Wis. 9. also, Flynn v. Brooklyn City R. Co., 9 App. Div. 269, 158 N. Y. 493.

Failure to sue on behalf of other stockholders is a mere defect of parties, and is waived if objection is not taken by answer or de-murrer. Stewart v. Erie & Western Transp. Co., 17 Minn. 372; Hiscock v. Lacy, 9 Misc. Rep. (N. Y.) 578, 30 N. Y. Supp. 860.

450 Forbes v. Memphis, El Paso & P. R. Co., 2 Woods, 323, Fed. Cas. No. 4,926; Prouty v. Michigan Southern & Northern Indiana R. Co., 1 Hun. (N. Y.) 655; Wood v. Union Gospel Church Building

Ass'n, 63 Wis. 9.

451 Simpson v. Westminster Palace Hotel Co., 8 H. L. Cas. 712; Russell v. Wakefield Waterworks relief which will inure to the bene-fit of all the stockholders, although in form a suit in behalf of the plaintiff alone, is in behalf of all, R. Co., L. R. 20 Eq. 474, 1 Smith's Cas. 291, 1 Cum. Cas. 725, per Sir G. Jes-sel, M. R.; Hoole v. Great Western plaintiff alone, is in behalf of all, R. Co., 3 Ch. App. 262, 2 Keener's and any stockholder may become Cas. 1302; March v. Eastern R.

When a stockholder sues to set aside or enjoin ultra vires transactions, or to enforce any right belonging to the corporation. or to redress or enjoin any injury to the corporation, the corporation is a necessary party defendant, so that any judgment rendered may be binding upon it; and if it is not made a party, the bill or complaint is demurrable. "Such a suit can only be maintained on the ground that the rights of the corporation are involved. These rights the individual shareholder is allowed to assert in behalf of himself and associates, because the directors of the corporation decline to take the proper steps to assert them. Manifestly the proceedings for this purpose should be so conducted that any decree which shall be made on the merits shall conclude the corporation. This can only be done by making the corporation a party defendant. The relief asked is on behalf of the corporation, not the individual shareholder, and if it be granted the complainant derives only an incidental benefit from it. It would be wrong, in case the shareholder were unsuccessful, to allow the corporation to renew the litigation in another suit, involving precisely the same subject-matter. To avoid such a result, a court of equity will not take cognizance of a bill brought to settle a question in which the corporation is the essential party in interest, unless it is made a party to the litigation.",452

Co., 43 N. H. 515; Tomkinson v. Southeastern Ry. Co., 35 Ch. Div. Insurance & Trust Co. v. Sebring, 5 675, 1 Smith's Cas. 300; Davis v. Rich. Eq. (S. C.) 342; Black v. Hug-Congregation Beth Tephila Israel, 40 App. Div. (N. Y.) 424.

452 Davenport v. Dows, 18 Wall. (U. S.) 626, 1 Smith's Cas. 280, 2 427; Foote v. Linck, 5 McLean, Keener's Cas. 1631, 1 Cum. Cas. 616, Fed. Cas. No. 4,913; Bell v. 3 Paige (N. Y.) 222, 233, 24 Am. Bruch, 54 Fed. 216, 56 Fed. 416; Dec. 212, 217; Greaves v. Gouge, 69 N. Y. 154; Brinckerhoff v. Bostwick, 88 N. Y. 52; Bell v. Mali, 11 How. Pr. (N. Y.) 254; Cunning-Linckerhoff v. Bostwick, 88 N. Y. 52; Bell v. Mali, 11 How. Pr. (N. Y.) 254; Cunning-Linckerhoff v. Bostwick, 88 N. Y. 52; Bell v. Mali, 11 How. Pr. (N. Y.) 254; Cunning-Linckerhoff v. Bostwick, 88 N. Y. 57; Brinckerhoff v. Bostwick, 88 N. Y. 52; Bell v. Mali, 11 How. Pr. (N. Y.) 254; Cunning-Linckerhoff v. Bostwick, 88 N. Y. 57; Brinckerhoff v. Bostwick, 88 N. Y. 57; Brinckerhoff v. Bostwick, 88 N. Y. 56; Brinckerhoff v. Bostwick, 88 N. Y. 57; Brinckerhoff v. Bostwick, 88 N. Y. 57; Brinckerhoff v. Bostwick, 88 N. Y. 56; Brinckerhoff v. Bostwick, 88 N. Y. 57; Brinckerhoff v. Bostwick, 88 N. Y. 52; Bell v. Mali, 11 How. Pr. (N. Y.) 254; Cunning-Linckerhoff v. Bostwick, 88 N. Y. 52; Bell v. Mali, 11 How. Pr. (N. Y.) 254; Cunning-Linckerhoff v. Bostwick, 88 N. Y. 57; Brinckerhoff v. Bostwick, 88 N. Y. 57; Brinckerhoff v. Bostwick, 88 N. Y. 52; Bell v. Mali, 11 How. Pr. (N. Y.) 254; Cunning-Linckerhoff v. Bostwick, 88 N. Y. 52; Bell

If a corporation is in the hands of a receiver at the time of a stockholder's suit, the receiver, as he represents the corporation, is a necessary party.453

If a suit brought by a stockholder on behalf of himself and the other stockholders is based upon fraudulent or wrongful acts or neglect on the part of the directors or other stockholders, they must be made parties defendant, so that they may have an opportunity to defend, and so that redress or relief may be given against them.454

If the subject-matter of the suit is an agreement between the corporation acting by its directors or managers and some other corporation or some other person, strangers to the corporation, it is proper and necessary to make such other corporation or person a party defendant to the suit, "because that other corporation or person has an interest, and a great interest, in arguing the question and having it decided, once for all, whether the agreement in question is really within the powers or without the powers of the corporation of which the corporator is a mem-

173; Cicotte v. Anciaux, 53 Mich. 227; Coxe v. Hart. 53 Mich. 557; Elkins v. Camden & Atlantic R. Co., 36 N. J. Eq. 241; Gruen v. Schoeffer, 7 Mo. App. 587; Crumlish's Adm'r v. Shenandoah Valley R. Co., 28 W. Va. 623.

A foreign corporation is not a necessary party to an action brought by one of its stockholders, on behalf of himself and the others, against a domestic corporation having property or debts owing or belonging to the foreign corporation, where the bill shows that the latter has ceased to use its franchise and been dissolved. Crumlish's Adm'r v. Shenandoah Valley R. Co., 28 W. Va. 623.

453 Porter v. Sabin, 149 U. S. 473.

60 Am. Rep. 245; Ribon v. Chicago, Rock Island & P. R. Co., 16 Wall. corporation and majority stock-(U. S.) 446; East Rome Town Co. holders, and the directors were v. Nagle, 58 Ga. 474; Westcott v. merely the defendants' instru-

Minnesota Mining Co., 23 Mich. 145; Tutwiler v. Tuskaloosa Coal, Iron & Land Co., 89 Ala. 391; Gray v. Fuller 17 App. (N. Y.) 29; Taylor v. Holmes, 14 Fed. 498; Ervin v. Oregon Railway & Navigation Co., 27 Fed. 625; Moyle v. Landers (Cal.) 21 Pac. 1133.

Compare Anderton v. Wolf, 41 Hun (N. Y.) 571.

The directors are not necessary parties in a suit to enjoin the corporation from doing an ultra vires act, or to set aside an ultra vires act, or to set aside an ultra vires act, for they merely represent the corporation. Winch v. Birkenhead, Lancashire & C. J. Ry. Co., 5 De Gex & S. 562; Bagshaw v. Eastern Union Ry. Co., 7 Hare, 114; Allen v. New Jersey Southern R. Co., 49 And see Swope v. Villard, 61 Fed. How. Pr. (N. Y.) 14; Pioneer Gold 417.

Mining Co. v. Baker, 20 Fed. 4; Wood v. Union Gospel Church Orleans Transp. Co., 91 Mo. 217, Building Ass'n, 63 Wis. 9.

Where the suit is against the

ber."455 Furthermore, such other corporation or person will not be bound by the decree that may be rendered, unless made a party.

## § 555. Judgment or decree as a bar.

When a stockholder brings a suit in equity in behalf of himself and other stockholders who may come in, to redress an injury to the corporation, making the corporation a party, as he must do, any judgment or decree rendered in the suit is clearly binding upon all who are parties to the suit, the stockholder suing and other stockholders who actually come in and become parties, the corporation itself, guilty officers who are made parties defendant, and third persons who may have participated in the wrongs complained of, and who are made parties defendant. Further than this, the judgment or decree, unless collusive, being binding upon the corporation, which is the real party in interest, and which represents not only the stockholder suing, but all other stockholders as well, is conclusive against all the other stockholders, whether they avail themselves of their right to come in and be made parties, or not; and they cannot afterwards bring another suit for the purpose of litigating the same ques-"From the very form and nature of these suits, each stockholder must be considered as represented, for if he is in sympathy with the complainant he may become a party complainant by application to the court; if he is in sympathy with

ments, and no relief is sought R. Co., 36 N. J. Eq. 241; Ribon v. against them, the directors need Chicago, Rock Island & P. R. Co., not be made parties. Woodroof v. Howes, 88 Cal. 184. See, also, Morse v. Bay State Gas Co., 91 ace-Car Co., 99 Fed. 168.

16 Wall. (U. S.) 446; Meyers v. Scott, 50 Hun (N. Y.) 603.

In a suit by a stockholder to Fed. 944; Eldred v. American Pal- compel restitution of assets alleged to have been fraudulently trans-<sup>455</sup> Sir G. Jessel, M. R., in Rusferred to the defendants, it is not sell v. Wakefield Waterworks Co., necessary to join as parties defend-L. R. 20 Eq. 474, 1 Smith's Cas. 291, ant the persons by or through L. R. 20 Eq. 474, 1 Smith's Cas. 291, and the persons by or through 1 Cum. Cas. 725; Salomons v. whom the transfer was made, or a Laing, 12 Beav. 377, 144 Jur. 471; person who holds some of the as-Hare v. London & North-Western sets as a mere depositary, and sub-Rv. Co.. 1 Johns. & H. 252; Peaject to the orders of the defend-body v. Flint, 6 Allen (Mass.) 52, ants, when no relief is sought 1 Smith's Cas. 263. 1 Cum. Cas. against them. Eldred v. American 795; Elkins v. Camden & Atlantic Palace-Car Co.. 99 Fed. 168. the threatened action of the company, he is represented by and in the corporation which is a necessary party to the suit. Not only this, but the court may, if satisfied that the interests of the corporation are not being properly presented or protected, admit a stockholder to be made a party defendant.456

Where a corporation is a party to an action involving the validity of a conveyance or other contract by it, the judgment or decree therein is a bar to a subsequent suit by a stockholder of the corporation to attack the same transaction.457

# § 556. Appointment of receiver-Winding up or dissolution of corporation.

There are express statutory provisions in some states under which a stockholder may sue for the appointment of a receiver and a winding up or dissolution of the corporation under circumstances specified in the statute. 458 And there may be very excep-

456 Willoughby v. Chicago Junc-Co., 50 N. J. Eq. 656, 1 Smith's Cas. 294, 2 Keener's Cas. 1656. Fed. 97.

457 Alexander v. Donohoe.

Hun (N. Y.) 131.

458 In New York, provision is made by statute for an action to procure a judgment dissolving a corporation:

solvent for at least one year.

(2) Where it has neglected or refused, for at least one year, to pay and discharge its notes or other evidences of debt.

(3) Where it has suspended its ordinary and lawful business for at

least one year.

(4) If it has banking powers, or power to make loans on pledges or deposits, or to make insurances, where it becomes insolvent or un-

The action may be maintained by tion Railways & Union Stockyards the attorney general in the name and in behalf of the people, or by a creditor or stockholder, on ob-And see Dannmeyer v. Coleman, 11 taining leave of the court, if the attorney general omits for sixty 68 days to commence the action, after submission by the creditor or stockholder of a verified statement of facts showing grounds for the action. Id. § 1786.

In such action, an injunction (1) Where it has remained in- may be issued to preserve the assets of the corporation pendente lite, and a receiver may be appointed. Id. §§ 1787, 1788. As to the

procedure in such action, see Id. §§ 1787-1796.

In Code Civ. Proc. N. Y. §§ 2419-2431, provision is made for proceedings for the voluntary dissolution of a corporation, on petition of a majority of the directors, trustees, or other officers having the able to pay its debts, or has violated any provision of the act by or fects, and other property thereof under which it was incorporated, or of any other act binding upon it. Code Civ. Proc. N. Y. § 1785. management of its concerns, if

tional circumstances under which a court of equity may appoint a receiver and wind up a corporation at the suit of a stockholder, even in the absence of a statute. 459 Ordinarily, however, a court of equity has no jurisdiction to dissolve a corporation at the suit of a stockholder, unless by virtue of some express statutory provision.460

Whether a court of equity may appoint a receiver in a stockholder's suit, not for the purpose of dissolving the corporation, but merely for the purpose of preserving the assets of the corporation, and preventing irreparable loss or injury pending the suit, is a very different question; and it is well settled that such power exists, as it does in the case of a partnership, if the circumstances render its exercise necessary. If it were otherwise.

those who may deal with it; or if, are affected, if he participated or for any reason, they deem it beneficial to the interests of the stockholders, that the corporation should be dissolved." Section 2420 prescribes the procedure when the directors or trustees are equally divided, etc. See, as to these sections, Hitch v. Hawley, 132 N. Y. 212, and cases cited ante, §§ 308, 319, 320,

A statute giving the courts jurisdiction, on petition of an officer or stockholder of a corporation, to require an accounting by its directors as to their official conduct, to remove them for gross misconduct, this own will and choice, regardless and require the election of others, and, incidentally, to appoint a receiver to take charge of the business of the corporation, does not authorize the winding up of a solvent corporation, and the distribution of its property. Sidway v. Missouri Land & Live-Stock Co., 101 Fed. 481.

A stockholder, under the Illinois statute, cannot enforce dissolution of a corporation or forfeiture of its charter, on the ground that it is an illegal combination or trust Mich. 97, 2 Cum. Cas. 234. prejudicial to the public. The state alone can complain on this ground. Nor can he do so for illegal acts,

acquiesced therein. Coquard v. National Linseed Oil Co., 67 Ill. App. 20, 171 Ill. 480.

It was held, under a Massachusetts statute, that it was no ground for dissolving a manufacturing corporation, on the petition of a majority in number of the stockholders owning a minority of the stock, that one owner of the majority of the stock had for many years controlled the election of officers, and elected himself agent and clerk; that he had for a long time managed the business "according to of the wishes and interests of the other stockholders;" that, according to his statement, the corporation had been doing a losing business for many years; that he had refused to make any change in the business, or to purchase the shares of the petitioners; and that, if the business were skillfully and properly managed, it might be made a source of profit to all concerned. Pratt v. Jewett, 9 Gray (Mass.) 34.

459 Miner v. Belle Isle Ice Co., 93

460 Ante, § 320; Neall v. Hill, 16 Cal. 145, 76 Am. Dec. 508; Wallace v. Pierce-Wallace Publishing Co., even when his individual interests 101 Iowa, 313, 63 Am. St. Rep. 389.

a stockholder would often be practically without any adequate remedy at all. Under statutes in some states, and independently of any statutes in others, the court may appoint a receiver in a stockholder's suit if the directors and majority of the stockholders are so managing or disposing of its business or assets in their own interest that they will probably be lost or destroyed before a decree can be rendered, or where there are such dissensions within the corporation that its business cannot be honestly or properly managed, or if for any other reason it clearly appears to the court that the appointment of a receiver pending the suit is necessary to preserve the assets of the corporation, and protect the rights of the complaining stockholders. 461 Without such a showing as this, however, a court will not appoint a receiver at the suit of a minority stockholder, and thus take the management

461 Featherstone v. Cooke, L. R. 16 Eq. 298; Sternberg v. Wolff, 56 N. J. Eq. 389, 67 Am. St. Rep. 494; Dickerson v. Cass County Bank, 95 Iowa, 392; Wallace v. Pierce-Wallace Publishing Co., 101 Iowa, 313, 63 Am. St. Rep. 389; In re Belton, 47 La. Ann. 1614; Davis v. United States Electric Power & Light Co., 77 Md. 35; Du Puy v. Transporta-tion & Terminal Co., 82 Md. 408; Miner v. Belle Isle Ice Co., 93 Mich. 97, 2 Cum. Cas. 234; Becker v. Gulf City Street Railway & Real Stevens v. Davison, 18 Grat. (Va.)

v. American Grocery Co., 80 Fed. 70; Darragh v. H. Wetter Mfg. Co. (C. C. A.) 78 Fed. 7; D. A. Tompkins Co. v. Catawba Mills, 82 Fed. 780; Powers v. Blue Grass Building & Loan Ass'n, 86 Fed. 705; Griffing v. A. A. Griffing Iron Co., 96 Fed. 577; Clark v. National Linseed Oil Co. (C. C. A.) 105 Fed. 787; Texas Consolidated Compress & Mfg. Ass'n v. Storrow (C. C. A.) 92 Fed. 5; Arents v. Blackwell's Durham Tobacco Co., 101 Fed. 338; Young v. Rutan, 69 Ill. App. 513; Estate Co., 80 Tex. 475; Bridgeport Jasper Land Co. v. Wallis, 123 Ala. Development Co. v. Tritsch, 110 652; In re Moss Cigar Co., 50 La. Ala. 274; Order of Iron Hall v. Ann. 789; Sincer v. Alverson, 51 Baker, 124 Ind. 293; Wayne Pike La. Ann. 955; Marcuse v. Gullett Co. v. Hammons, 129 Ind. 368; Gin Mfg. Co., 52 La. Ann. 1383; Ann. 789; Sincer v. Alverson, 51 La. Ann. 955; Marcuse v. Gullett Gin Mfg. Co., 52 La. Ann. 1383; Empire Hotel Co. v. Main, 98 Ga. Stevens v. Davison, 18 Grat. (Va.)
819, 98 Am. Dec. 692; State v. Second Judicial District Court of Silver Bow County, 15 Mont. 324, 48
Am. St. Rep. 682; Aiken v. Colorado River Irrigation Co., 72 Fed. 591; Stewart v. Belt (Miss.) 19 So. 957; In re Lewis, 52 Kan. 660; Halpin v. Mutual Brewing Co., 91 Hun (N. Y.) 220; Piza v. Butler, 90 Hun (N. Y.) 220; Piza v. Butler, 90 Hun (N. Y.) 254; Osgood v. Maguire, 61 N. Y. 524.

See, also, as to the appointment of a receiver at the suit of a stockholder or stockholders, Becker v. Maine Real Estate Co., 93 Me. 324; Hoke (C. C. A.) 80 Fed. 973; Hunt of the corporation out of the hands of its directors and stockholders, even for a limited time, although the latter may be charged with fraud and mismanagement. 462

ney v. Detroit & Montana Cattle Co. v. Hooper, 105 Ala. 665; Mason Co., 116 Mich, 640; People's Investment Co. v. Crawford (Tex. Civ. App.) 45 S. W. 738; Cameron v. Groveland Improvement Co., 20 Wash, 169. 462 Waterbury v. Merchants' Union Express Co., 50 Barb. (N. Y.) 157; People v. Albany & Susquehanna R. Co., 55 Barb. (N. Y.) 344; Wallace v. Pierce-Wallace Publishing Co., 101 Iowa, 313, 63 Am. St. Rep. 389; Peatman v. Centerville Light, Heat & Power Co., Rumney v. Detroit & Montana Cat-100 Iowa, 245; Hyde Park Gas Co. tle Co., 116 Mich. 640; Stockton v. v. Kerber, 5 Ill. App. 132; Down- Harmon, 32 Fla. 312; ing v. Dunlap Coal, Iron & Railway Hotel Co. v. Main, 98 Ga. 176; Co., 93 Tenn. 221; Fischer v. Su- Steele Lumber Co. v. Laurens perior Court of City & County of Lumber Co., 98 Ga. 329; Crombie v. San Francisco, 110 Cal. 129; Ein- Order of Solon, 157 Pa. St. 588; stein v. Rosenfeld, 38 N. J. Eq. 309; Flunker v. Emporia City Ry. Co., Fort Payne Furnace v. Fort Payne 48 Kan. 557. And see the cases Coal & Iron Co., 96 Ala. 472, 38 Am. cited in note 461, supra.

Investment Co., 138 Mo. 408; Rum- St. Rep. 109; Little Warrior Coal v. Supreme Court of Equitable League, 77 Md. 483, 39 Am. St. Rep. 433; Edison v. Edison United Phonograph Co., 52 N. J. Eq. 620; Laurel Springs Land Fougeray, 50 N. J. Eq. 756; Wenzel v. Palmetto Brewing Co., 48 S. C. 80; New Birmingham Iron & Land Co. v. Blevens, 12 Tex. Civ. App. 410; People's Investment Co. v. Crawford (Tex.) 45 S. W. 738; Cicotte v. Anciaux, 53 Mich. 227;

